The Economist

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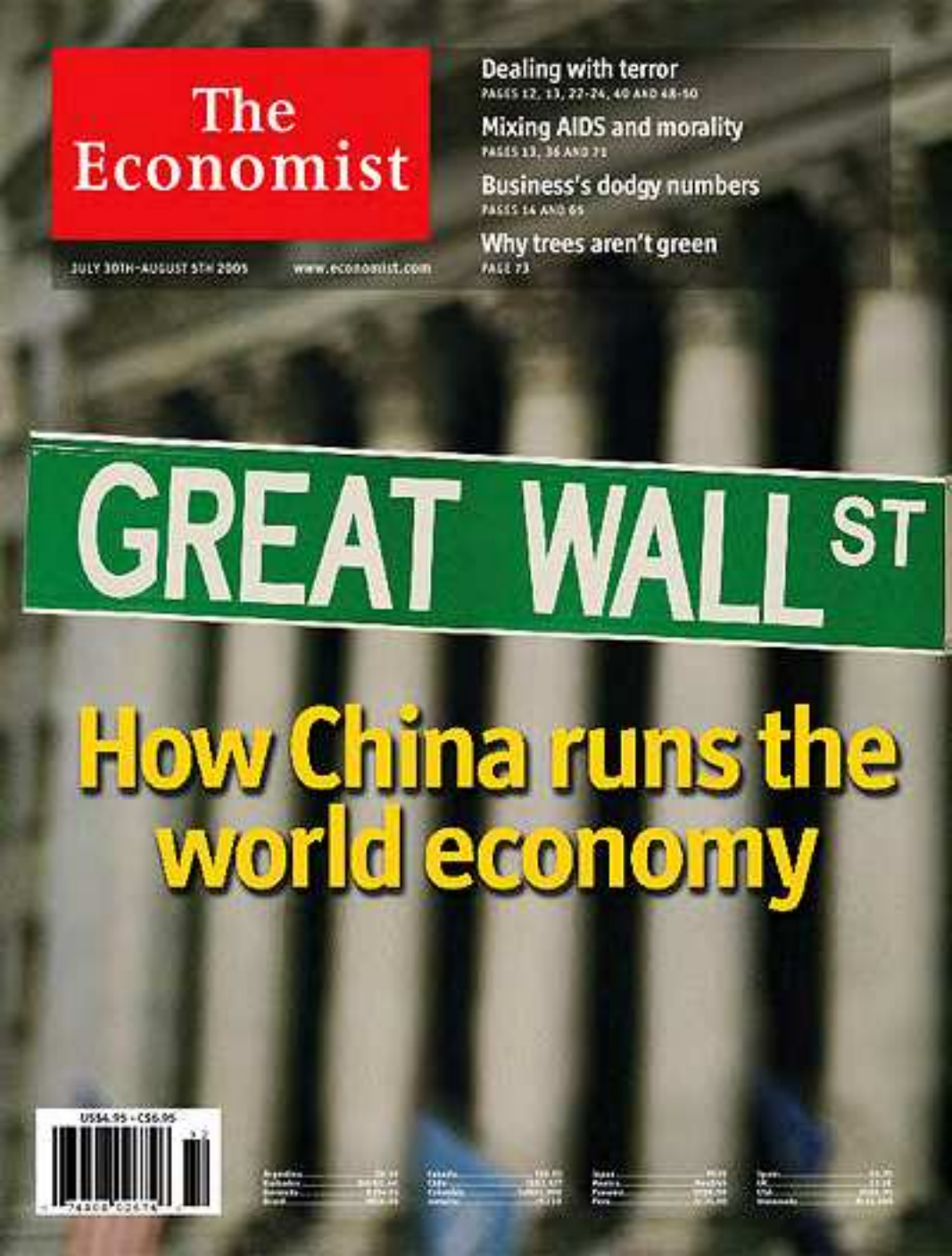

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Politics this week

Jul 28th 2005
From The Economist print edition

AP

Suicide bombings in Egypt

Three suicide-bombers in Sharm el-Sheikh, an **Egyptian** resort on the Red Sea, killed at least 67 Egyptians and foreigners. It was uncertain who the perpetrators were or whether they had international links. Suspicion fell on a network of aggrieved Bedouin from the Sinai desert.

See article

Sunni Arab members of **Iraq's** constitutional drafting committee ended a boycott after the murder of two of their colleagues. Hopes rose that a draft could be presented to parliament ahead of schedule, next week.

See article

The Saharan country of **Mali**, as well as its neighbour, **Niger**, was reported to be suffering a famine; more than 4m people in both countries are said to be facing starvation.

See article

A UN report said that the **Zimbabwe** government's recent clearance of illegal urban dwellings and shops had left 700,000 people homeless and destitute. President Robert Mugabe, hoping for financial support, signed a deal with China for economic and technical co-operation.

See article

Swine fever

China said bacteria carried by pigs had killed 27 people and may have infected more than a hundred others in the south-western province of Sichuan. The bacteria, *streptococcus suis*, are commonly found in animals but do not normally cause illness in humans.

Gloria Arroyo, the **Philippines'** embattled president, used her state-of-the-nation address to call for a move from a presidential system to a parliamentary government. Her opponents have filed a motion for her impeachment for interference in the 2004 elections.

Over one thousand people held an anti-American protest outside the military base in Bagram, **Afghanistan**. Similar protests in May were triggered by reports that Americans had desecrated the Koran.

Kirgizstan agreed to allow America to keep its airbase in the country for as long as needed to prosecute the war on terror in Afghanistan. The government's announcement followed a joint communiqué from the Shanghai Co-operation Organisation, of which Kirgizstan is a member, demanding that American forces set a deadline for withdrawal from the region.

At a meeting in Laos of the Association of South-East Asian Nations, America and five other countries unveiled a new plan to combat **global warming**. The ASEAN meeting also heard that Myanmar would give up its turn to take the rotating chairmanship of the regional body.

See article

More to come?

Police investigating an unsuccessful attempt to detonate **bombs in London** on July 21st centred their inquiries in the city and in Birmingham, where one of the suspected bombers, Yasin Hassan Omar, was arrested. The attack followed the same pattern as the deadly explosions of July 7th, inviting speculation that the operations were planned by the same person. Jittery Londoners were not soothed by the killing of an innocent 27-year-old Brazilian, Jean Charles de Menezes, who was shot by police on the mistaken assumption that he was about to explode a bomb.

See article

In the Netherlands, Mohammed Bouyeri, who had confessed in court to killing **Theo van Gogh**, a controversial film-maker, and said he would be ready to do it again, was sentenced to life in prison without parole.

The **Irish Republican Army** made a formal declaration that it was ending its armed campaign to pursue peaceful politics, ending more than 30 years of violence.

See article

Israel's prime minister, Ariel Sharon**,** visited **France**, seeking to mend fences after he caused upset a year ago by suggesting that Jews should leave France because of anti-Semitism. France has praised Mr Sharon's plan to evacuate settlers from the Gaza strip.

The diplomatic war between **Belarus** and **Poland** hotted up. Belarus expelled the Polish *chargé d'affaires*. After Belarussian special forces raided offices of the Polish minority, Poland recalled its ambassador.

Turkey's prime minister, Recep Tayyip Erdogan, promised yet again to sign an extension of its customs union with the EU to cover Cyprus. But he insisted this did not imply recognition of the Greek-Cypriot government.

On message

The **Inter-American Development Bank** chose as its new president Luis Alberto Moreno, Colombia's ambassador to the United States. Mr Moreno, who was supported by the United States and was an architect of American aid to Colombia, easily defeated candidates from Brazil and Venezuela, among others.

Cuba's government arrested 30 dissidents; most were later released. Meanwhile, discontent is growing over power cuts, but Fidel Castro claimed that the island's economy will grow by 9% this year.

AFP

See article

Telesur, a regional television channel financed mainly by Venezuela's government and backed by Argentina, Cuba and Uruguay, began transmissions. The channel's director, Andrés Izarra, resigned as Venezuela's information minister after criticism that the station would be a mouthpiece for the country's president, Hugo Chávez.

See article

The wife of the businessman at the centre of **Brazil's** corruption scandal told a congressional panel that José Dirceu, who resigned last month as chief of staff to President Lula da Silva, knew of undeclared loans to the ruling Workers' Party. Brazil's currency and stockmarket have fallen in recent days over fears, hotly denied, that Lula himself may have known of illegal payments to legislators.

See article

The last time?

EPA

NASA grounded future shuttle flights after debris fell from its *Discovery* craft

during lift-off. It was the first manned space mission by NASA since the *Columbia* disaster in 2003.

Two of the largest **unions** in the AFL-CIO, America's labour federation, left the organisation because of bitter disagreement over the future of reforms. The Teamsters and the Service Employees International Union have a combined membership of 3.2m, a third of the AFL-CIO's total. More unions are expected to follow in the most damaging split to America's labour movement since the 1930s.

See article

Hillary Clinton upset her left-wing base by making a speech calling for a moderate Democratic agenda to fight the 2008 presidential campaign.

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Business this week

Jul 28th 2005
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DaimlerChrysler chief quits

DaimlerChrysler announced that its chief executive, Jürgen Schrempp, will step down at the end of this year. Mr Schrempp faced fierce criticism from shareholders in April about the performance of the company's Smart car division, which has suffered heavy losses, and quality control in the luxury Mercedes division. The company also reported a 20% drop in operating profit for the second quarter, compared with a year ago.

See article

The governor of **Italy's central bank**, Antonio Fazio, came under intense pressure to resign as the transcript of a tapped conversation between himself and the boss of **Banca Popolare Italiana** was made public. Italy's stockmarket regulator has suspended BPI's bids for Banca Antonveneta, a larger competitor. A rival offer by **ABN Amro**, a Dutch bank, failed last week. **Banco Bilbao Vizcaya Argentaria**, a Spanish bank, has admitted defeat in a separate bidding war for **Banca Nazionale del Lavoro.**

See article

Barclays completed the acquisition of a 54% stake in **Absa**, South Africa's biggest retail bank. The 28 billion rand ($4.2 billion) transaction, South Africa's largest foreign direct investment, was recently cleared by the country's courts. Activists had tried to block the British bank's move, arguing it owed reparations from dealings during the apartheid era.

Commerzbank confirmed that a top executive, who unexpectedly resigned last week, is at the centre of a money-laundering investigation being conducted by German and Swiss authorities. The inquiry is focused on transactions between the German bank and a Russian telecoms firm with connections to the Kremlin. Commerzbank's offices in Frankfurt were also searched last week.

Teva Pharmaceuticals, based in Israel, agreed to buy **Ivax**, a rival drugs company based in Miami, for $7.4 billion. Teva now trades places with Novartis to become the world's largest maker of generic drugs.

See article

Mixing politics with business

America's House of Representatives narrowly approved the **Central American Free Trade Agreement** by 217 votes to 215. This is the controversial deal's last legislative hurdle, and was cleared only after intense lobbying by President George Bush himself.

See article

France's stockmarket regulator, AMF, said it will investigate trading in shares of the food group **Danone**, which rose by 27% in the two weeks after feverish speculation began that **PepsiCo** was about to make a takeover bid. Meanwhile, Jacques Chirac criticised short-term investors for destabilising the long-term interests of French firms.

France Télécom acquired an 80% stake in **Amena**, Spain's third-largest mobile-phone operator, valuing the firm at *euro*10.6 billion ($12.7 billion). Debt-laden France Télécom now has access to Spain's fast-growing mobile market.

See article

EADS posted a net profit of *euro*816m ($979m) for the first half of the year, an increase of 114% compared with a year ago. The group said a strong performance from **Airbus**, of which it owns 80%, will help it beat its earnings target for the year. **Boeing**, Airbus's rival, said it also expected to exceed its yearly forecast on the strength of recent aircraft orders, but reported that net profit for the second quarter had fallen by 7%, to $566m (revenue increased by 15%).

Flying into oblivion?

Northwest Airlines warned unions and politicians that it faced a real threat of bankruptcy unless it could cut $1.1 billion in labour costs. America's fourth-biggest carrier made a second-quarter net loss of $225m, compared with a loss of $182m a year ago.

Amazon said that tax charges in the second quarter had reduced net profit by 32%, compared with the same period in 2004, to $52m. However, sales increased by 26% to $1.75 billion, delighting investors worried about the online retailer's discounting scheme. Amazon's shares rose by 10%.

Netflix, an online DVD-rental company, reported a 97% increase in net income for the second quarter and said it expected to make a profit for the whole year, rather than the loss it had previously forecast.

Lexmark, which makes printers for personal computers, reported a 42% fall in net profit for the second quarter, compared with a year ago. The firm was hit by a tax charge, but also blamed fierce competition from Hewlett-Packard.

Fröhlich?

German business confidence is at its highest level since February, according to Ifo, a think-tank. Firms hope that a weaker euro will drive exports and that labour reforms will bring lower wage claims. Germany's consumers take a more pessimistic view. GfK, a research firm, said it expects consumer sentiment in August to drop again, partly on fears that income will fall.

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Letters

Jul 28th 2005
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Farming the land

SIR – You illustrate the difficulties of creating viable new black-owned farms through land reform in South Africa ("Should reform be faster or steadier?", July 9th). Almost every measure enacted by government to protect and help poor black farmers has ended up impoverishing them even further. For instance, a farm co-operative programme was created in the 1990s, but the initiative failed because of a lack of full property rights attached to newly acquired land. Authorities feared that, left to their own devices, co-ops might sell their land back to white farmers, so they made it impossible for them to do so. A project I recently managed in Limpopo, which aimed to salvage about 25 co-op farms, proposed that the co-ops be transformed into corporations and enter into joint-ventures with white commercial farmers. The provincial agriculture department rejected the idea as a cover for restoring white ownership.

For land reform to succeed, property rights must be absolute. The willing buyer-seller principle is a critical part of that, but the new owners must also have full rights that enable them to sell their land; these rights cannot coexist with a paternalistic system telling them what they may or may not do with their property. Only by granting full property rights will South Africa be able to create a class of independent black landowners and thus avoid replicating Zimbabwe's tragic example.

Charles Krakoff
Koios Associates
Acton, Massachusetts

Carbon markets

SIR – Your report on nuclear power rightly argues for carbon taxes as the best way to tackle climate change ("The shape of things to come?", July 9th). But you say that even a moderate carbon tax would not make nuclear power competitive, noting that the price of permits in Europe's emissions-trading scheme implies a social cost of carbon dioxide of *euro*20 per tonne. This would be correct only if we could be confident that the right number of permits had been issued, which unfortunately we cannot be. A better method is to attempt to estimate the social cost of carbon dioxide directly, difficult though this is.

The study you mentioned, by the British government in 2002, proposed a value of £70 (*euro*112) per tonne. However, this was actually the value found per tonne of carbon, which converts to only about £20 per tonne of carbon dioxide. This slightly higher figure is unlikely to have a great effect on the economics of nuclear power. What might make a difference is that the social cost of carbon dioxide will grow over time as we begin to experience more severe impacts from climate change. Our best estimate at the moment is that the social cost grows by about 2.5% per year, so that preventing carbon dioxide emissions in 30 years time will be more than twice as valuable as preventing them today. This would be well within the operating lifetime of any nuclear plants, even if we took the decision to start building them today.

Chris Hope
Cambridge, Cambridgeshire

SIR – Given the abundance and long-term availability of coal to the major economies of the world, both developed and emerging, it is clear that there would be immense benefit in developing technologies that will enable the widespread use of coal with near zero emissions. Such technologies are hardly new but

now need to be made commercial on a large scale. The future of the world lies not merely in safe nuclear power, but in a mix that includes cheap and reliable renewables and clean coal. Each of these is a hard task, but worthy of action by government and meets our energy needs for this century.

Milton Catelin
World Coal Institute
London

SIR – Your article on Europe's new carbon markets suggests that the number of carbon trades determines whether these markets "reverse global warming" ("Revving up", July 9th). Actually, global warming is inherently irreversible. But large reductions in carbon emissions would ameliorate climate change's impact, whether or not there are large volumes of trades. The volume of trading increases the amount of cost savings, not the amount of reductions.

David Driesen
Syracuse, New York

A dog's life

SIR – Greyhound racing ought to be abolished, not given a "makeover" ("Gone to the dogs", July 16th). Over half of all greyhounds are killed after spending a hard life muzzled and pent-up in small kennels between 18 and 22 hours a day. Many of them die of starvation or electrocution, are shot or are sold for medical and biological experiments. These are excellent reasons why greyhound racing is going out of business and why several states have recently made it illegal. Gambling is not one of humanity's more dignified activities to begin with, but when it is combined with cruelty to gentle, innocent animals, it is abhorrent.

Dan Cudahy
Avon, Colorado

Device and virtue

SIR – I'm not sure I wholly agree with your portrayal of BlackBerry users as "addicts"— strung-out slaves to their devices, lives in tatters, praying for the 12-step programme that will break their cycle of dependence ("The CrackBerry backlash", June 25th). Could it be that we actually enjoy our work and corresponding with colleagues and clients more than we care to admit? Perhaps the stolen BlackBerry moment at home, at the weekend or on holiday is actually a temporary respite from screaming children or nagging spouses—a moment of calm in the chaos of our personal lives. My BlackBerry listens well, never talks back, respects my authority, goes to sleep when I want and nags me only when I ask it to. And you wonder why we are addicted! Sent, naturally, from my BlackBerry wireless.

Jim McDonnell
London

Not even a postcard

SIR – Your speculation on the early 15th-century voyages of Chinese admiral Zheng He misses the real story ("The admiral of what might have been", July 16th). The reason why this sea-going eunuch fell from favour was because he brought nothing back from his adventures to cover the staggering costs of his missions. No Chinese emperor, or European king for that matter, would pay indefinitely for voyages of discovery without expecting some return. Columbus may have opened the way for somebody else to find Peruvian silver, but he had promised only Indian spices and at least brought something back. The Chinese, to the contrary, had to wait for a century after Zheng He to sell their tea to the Dutch in Batavia. The Chinese expeditions were nothing more than luxury tourist cruises. Trade or perish: that is the history of mankind in a nutshell.

Bo Herman
Rotterdam

Positions of power

SIR – Lexington writes that "Bill Clinton was brought to his knees by Monica Lewinsky" (July 16th). I had always thought it was the other way around, the vice, in this case, being versa.

Budd Whitebook
Washington, DC

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International economics

How China runs the world economy

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From The Economist print edition

Global wages, profits, prices and interest rates are increasingly being influenced by events in China

"IF YOU want one year of prosperity, grow grain. If you want ten years of prosperity, grow trees. If you want 100 years of prosperity, grow people." This old Chinese proverb crudely sums up how the entry of China's massive labour force into the global economy may prove to be the most profound change for 50, and perhaps even for 100, years.

China, along with the other emerging giants, India, Brazil and the former Soviet Union, has effectively doubled the global labour force, hugely boosting the world's potential output and hence its future prosperity. China's growth rate is not exceptional compared with previous or current emerging economies in Asia, but China is having a more dramatic effect on the world economy because of two factors: not only does it have a huge, cheap workforce, but its economy is also unusually open to trade. As a result, China's development is not just a powerful driver of global growth; its impact on other economies is also far more pervasive (see article).

Beijing's new influence was clear from the shockwaves in global currency, bond and commodity markets last week after it announced that the yuan will no longer be pegged to the dollar. Until a couple of years ago nobody cared much that the Chinese yuan was pegged to the dollar. Recently, though, this link has become one of the hottest issues in international politics, widely blamed in America for its huge trade deficit.

Last week's 2.1% revaluation of the yuan is trivial and unlikely to dent America's trade deficit. More important is the breaking of the yuan's formal link to the dollar and the shift to a so-called "managed float" against a basket of currencies. In theory, this allows considerable scope for a further rise in the yuan against the dollar, though it is unclear by how much the Chinese authorities will allow the yuan to climb.

Even if last week's adjustment was timid, it could mark an important turning point. It is certainly a step in the right direction for China itself, as greater currency flexibility will give it more room to use monetary policy to steer the economy. More interesting are the implications for the world economy. This might be the beginning of the end of what has been dubbed a revived Bretton Woods system of fixed exchange rates between China (and other Asian economies) and America.

The dragon's breath

Under this arrangement, China has provided cheap finance to America's consumers and its government by buying Treasury bonds. If the switch to a currency basket causes China to reduce its new purchases of dollar assets, then American bond yields could rise. America's China bashers, who demand a further revaluation of 25% or more, should therefore be careful. Such a large-scale revaluation would surely push bond yields higher and badly hurt America's economy. Indeed, if the yuan's adjustment has any real impact on America's trade deficit, it will not be through the revaluation itself, but because higher bond yields squeeze domestic demand.

America's trade deficit is due mainly to excessive spending and inadequate saving, not to unfair Chinese competition. If China has contributed to America's deficit it is not through its undervalued exchange rate, but by holding down bond yields and so fuelling excessive household borrowing and spending. From this point of view, global monetary policy is now made in Beijing, not Washington.

Puzzle key

The popular focus on the yuan, America's trade deficit and jobs as China's main impact on the rest of the world misses the point. China's growing influence stretches much deeper than its exports of cheap goods: it is revolutionising the relative prices of labour, capital, goods and assets in a way that has never happened so quickly before. A recognition of China's profound and widespread impact on the world economy explains various current economic puzzles.

Take, for instance, the oil price. Since the beginning of last year, oil prices have doubled, yet in contrast to previous oil shocks, inflation rates remain low and global growth robust. The answer to this riddle is China. To the extent that oil prices are driven up by strong Chinese demand rather than, as in the past, an interruption of supply, they are less likely to hurt global growth. And the impact of higher oil prices on inflation has been offset by falling prices of all sorts of goods from cameras and computers to microwaves and bicycles—thanks to China. In addition, competition from China and the threat that firms in developed countries might shift offshore also helps to keep a lid on wages and hence inflation.

Another oddity is that, while the prices of most goods are falling, house prices are soaring in many countries. Again, enter the dragon. Cheaper goods from China have made it easier for central banks to achieve their inflation goals without needing to push real interest rates sharply higher. This has encouraged a borrowing binge. The resulting excess liquidity has flowed into the prices of assets, such as homes, rather than into traditional inflation. And, last but not least, there is the conundrum which has puzzled Alan Greenspan, head of America's central bank: why are American bond yields so low despite robust growth and hefty government borrowing? Part of the answer lies, once again, with China, which has bought large quantities of Treasury bonds to hold down its currency.

Over the coming years, developed countries' inflation and interest rates, wages, profits, oil and even house prices could increasingly be “made in China”. How should the world's policymakers respond to China's growing economic clout? Trying to halt China's growth through protectionist measures, as many American congressmen would like to do, would be a disaster, for it would close off a powerful source of future global prosperity.

A better way to deal with China's growing power would be to give the country a bigger stake in global economic stability. China should be a full member of international economic policy forums, such as the G7 and the OECD. Western policymakers would be wise to remember another Chinese proverb: “What you cannot avoid, welcome.”

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Terrorism

The new face of London's police

Jul 28th 2005
From The Economist print edition

Policemen and politicians are shooting from the hip. That's bad

LONDONERS are living under a shadow. Nine bombs since July 7th in the hands of young men who without warning sought to take as many lives as they could—including their own—represent an alarming new threat. One lethal shooting, of an innocent Brazilian man by London's Metropolitan Police on July 22nd, bears witness to the perils of the response.

In extraordinary times countries seize on extraordinary measures. The police marksmen who gunned down Jean Charles de Menezes in an underground train were acting under procedures designed to stop a suspected suicide-bomber before he detonates his charge—in the words of their former boss, to “destroy his brain instantly, utterly”. In the rush to arm itself against the bombers, the government this week laid the ground for emergency anti-terror legislation that includes powers to stop those training terrorists or planning an attack, to prosecute anyone “glorifying” or fomenting terror, and possibly to let police hold suspects for up to three months.

Because suicide attacks are new to Britain, it is right that the country should examine its defences. But Mr de Menezes's violent death contains two lessons—that the police and the security services will make full and frequent use of their “exceptional” powers, and that they will make mistakes.

Guard the guards

Since those first blasts, the police have on 250 separate occasions thought they might be dealing with a suicide-bomber, the chief of the Metropolitan Police reported this week. They have almost opened fire no fewer than seven times, Sir Ian Blair disclosed. His moral—that “we have got as close to calling it as ‘that’ and we haven't”—and news of an inquiry by the Independent Police Complaints Commission into the shooting were designed to be reassuring. Instead they suggest that, in the three to six months of the inquiry, police procedures that have once failed fatally will be tested thousands of times.

That matters because the police face some hard questions about Mr Menezes's shooting at Stockwell in south London. On what grounds was he followed as he left the only entrance of a block which contained not only a flat under surveillance, but many others beside? Why, if police thought he was dangerous enough to kill once he boarded a tube, was he first allowed to board a bus? Was he warned when he began to flee the (plainclothes) police pursuing him? When the new guidelines for shooting-to-kill suicide-bombers were introduced at the start of 2002, why weren't the public or Parliament told?

A YouGov poll for *The Economis*t shows overwhelming public support for the police and their tactics (see article). That is partly a well-deserved reflection on an investigation that has rapidly identified the terrorists. But the public should temper its gratitude with vigilance. Britons need to be sure that, if the investigation into Mr Menezes's death finds fault with the operation, police procedure and training will change, and that whoever is responsible will be held accountable.

It seems likely that the police over-reacted on the basis of poor information. Politicians do the same under pressure. Emergency legislation which is at first judged a triumph often turns out to be either authoritarian or foolish. The internment of suspected Irish terrorists without trial in the 1970s turned out to be counterproductive; Britain made itself a laughing stock when it gave employment to resting actors who were paid to read the words of banned Sinn Fein politicians.

We have seen the future

Good policing is about good information. Draconian or daft laws corrode the very links to Muslim Britain that the government and police say they need to combat terrorism. The new legislation will be drafted in haste, but is likely to remain in force for a long time. Although the second wave of bombs on London on July 21st failed to detonate, it carried a baleful message: bombings and manhunts will be part of British life for many years.

Which is why, as Britain contemplates new emergency powers, it needs to build in safeguards against the constant danger of mistakes and the police's tendency to make full use of their powers. One protection is for all new legislation and policy to require an annual revision. A ritual, perhaps, but one that creates the scope for debate and a reminder that what has come to be part of the furniture of law enforcement was once seen as a regrettable sacrifice of liberty to security.

For the same reason, new legislation should when possible be supervised by judges and, better, the courts. The three months sought by the police is too long to lock someone away without charge. The lengthy incarceration of an innocent young Muslim man (that, after all, is who would be confined) would destroy his faith in Britain and the loyalty of his family and friends. If there is a case for legislation to allow suspects to be held more than 14 days, the person to contain the security services' zeal is a judge.

But the best place for suspected terrorists is in the dock. That is a reason to help bring people to trial, by creating a new charge of acts preparatory to terrorism and also to overrule the security services and admit as evidence information from intelligence intercepts. There are ways to minimise the fear this will compromise intelligence operations.

The third safeguard is free speech. Nobody likes preachers spouting hate. Under today's laws a jury convinced that their words lead directly to violence can put them in jail. But the new laws would outlaw something far vaguer and harder to define—and sweep bookshops and websites into the net.

That is both foolish and draconian. Foolish because in an open society and the age of the internet such a ban on free speech would not work. Draconian because it elevates the *jihadis'* arguments. Are they so potent that they should be dignified by being banned? Are not the counter-arguments upon which British society is founded stronger? Nothing would be more beguiling to disillusioned Muslim youth than the illicit words of imams banished by British bureaucracy.

Tony Blair this week vowed that his government would yield “not one inch” to the terrorists. It just has.

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The IRA

A farewell to arms

Jul 28th 2005
From The Economist print edition

As one terrorist problem engulfs Britain, another subsides

Reuters

Get article background

IN POLITICS, even the violent politics of terrorism, timing can mean everything. On July 28th, the Irish Republican Army (IRA) at long last issued the statement for which most people in Britain and both parts of Ireland have been waiting for years. The IRA declared that its leadership had “formally ordered an end to the armed campaign”, and told all its units to “dump arms” and work through “exclusively peaceful means”. If it truly means a permanent end to Irish terrorism, then the statement will be as “historic” as Irish republicans are claiming. But even if the IRA means what it says, there are still many questions left unanswered.

Northern Ireland's unionists will be the loudest in voicing many of these. By the obfuscating standards of past IRA statements, this week's announcement is crystal clear. But unionists will point out that it does not contain the exact phrase “the war is over”, which is something that they have long sought, and it does not say explicitly that the IRA itself is disbanding, which is something they have long demanded. Both are fair points. And yet the IRA was never going to adopt the precise phraseology demanded by unionists. To all intents and purposes, the IRA has now officially ended its violent campaign, turning a prolonged ceasefire into a permanent halt.

The more important questions go beyond the critique of Northern Ireland's unionists. The first concerns the province itself. Can the IRA's statement break the stalemate in Ulster and help to establish something resembling a normal government? That is not clear (see article).

Five or six years ago, soon after the Good Friday Agreement of 1998, such a statement from the IRA would have been electrifying, and would probably have forced unionists into a power-sharing government. Today, 11 years after the IRA's first ceasefire and endless bitter arguments, it looks like too little, too late. The IRA is clearly trying to salvage the political fortunes of Sinn Fein, which have been badly tarnished by the IRA's own continuing criminal activity. For many in both parts of Ireland, the IRA's grand gesture will look like little more than a desperate ploy.

The second and bigger question is: what lessons does the IRA's abandonment of terrorism—or “armed struggle” as it always preferred to call it—hold for the task of combating and defeating today's more virulent forms of terrorism? Here the answer contains reasons for both optimism and pessimism.

The optimistic bit is that talking to terrorists can, sometimes, stop violence and bring peace. There was plenty of justified scepticism when the IRA first began to make its overtures to the British government in the early 1990s, and many strongly felt that speaking to bombers and assassins was not only morally reprehensible, but would not work. And yet the peace process has, after many ups and downs, brought real peace to Northern Ireland and a gradual halt to Irish terrorism.

Talking to the IRA was justified and effective, ultimately, because the unpalatable truth was that they were fighting for something that many in Northern Ireland believed was a legitimate goal—Irish unity. The IRA had an aggrieved constituency, which eventually realised that violence was getting it nowhere. Today's much more violent Islamic-inspired terrorism, by contrast, recognises no limits, makes no demands which can be addressed and seems to represent no one but the fanatics themselves. There is no point in talking to them. They can only be defeated.

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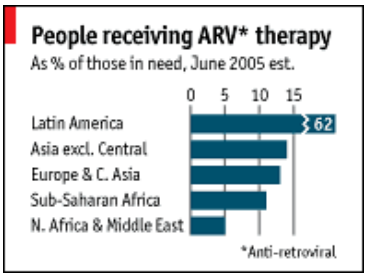
AIDS

Too much morality, too little sense

Jul 28th 2005
From The Economist print edition

Politicians must suspend moral judgments if AIDS is to be defeated

Get article background



THE world is not winning the war against AIDS. By the end of this year, 3m poor people infected with HIV, the virus that causes AIDS, are supposed to be receiving the treatment they need. So far, though, barely 1m are. At present, about 40m people are living with HIV, some 5m are infected with it each year and over 3m die from it. The human and economic cost is huge. India may well have more infected people than any other country. China's epidemic has the potential to dwarf all others (see article).

In most of the world, AIDS tends to affect fairly discrete groups, usually prostitutes, homosexuals and drug addicts. In most societies these people are frowned upon. Democracies like them no more than autocracies. When it comes to receiving help from taxpayers, they are never at the top of anyone's list, especially in countries so poor that basic health care is not available to most citizens.

But if AIDS is not contained among the groups that harbour it, it spreads into the general population, as it has in Africa. There, it affects every section of the population—slum-dweller and sophisticate, peasant and professional. Everyone who engages in that near universal activity, sex, is at risk. As it is, AIDS is no respecter of morals: it affects babies as they are born, children as they are orphaned, nurses as they are accidentally pricked by a dirty needle, patients of any kind as they receive a transfusion of contaminated blood. Indeed, it affects the entire society in which its victims live and die.

It also affects the faithful wife of the unfaithful husband. That is why the ABC slogan so beloved by the Bush administration—Abstinence, Be faithful and Condoms—is, in practice, a slap in the face to many people. The President's Emergency Plan for AIDS Relief commits at least a third of its promised $15 billion to “abstinence until marriage” as the main way of stopping the spread of AIDS. It also urges that the use of condoms be confined to people who engage in “risky behaviour”—prostitutes or couples with one member who is HIV-positive. Many groups are reported to be ending or reducing their condom-promotion schemes to qualify for American money.

That might not matter if condoms did not matter, but they do. In the absence of a proper vaccine, an absence that is likely to continue for years, condoms are the best prophylactic available to anyone at risk of HIV infection through a sexual encounter, within or outside marriage (see article). Abstinence might, it is true, be better still, but abstinence will not, in the real world, be practised widely enough to bring AIDS under control. Now, in a further demonstration of its moral zeal, the Bush administration is insisting that all groups, American or foreign, that are engaged in the struggle against AIDS must declare their opposition to prostitution if they are to receive American money. The administration is also against all needle-exchange projects for drug addicts, one of the groups most likely to contract, and spread, AIDS in Russia, India and China.

The poor countries that have got on top of nascent AIDS epidemics—Brazil (see article), Thailand, Uganda and Cambodia—have done it by changing behaviour. That is no easy task, involving as it does a variety of actions across a wide front. It has proved possible because limits have been set on the endeavour: people have not been asked to act morally, merely in their own self-interest, which happens to be in the interest of society.

The lesson for rich and poor alike is that to contain AIDS morality must take second place. Politicians may find it easier to yield to sanctimonious lobbyists than to explain why refraining from judging other people makes more sense. But that does not excuse them. Too many lives are at stake.

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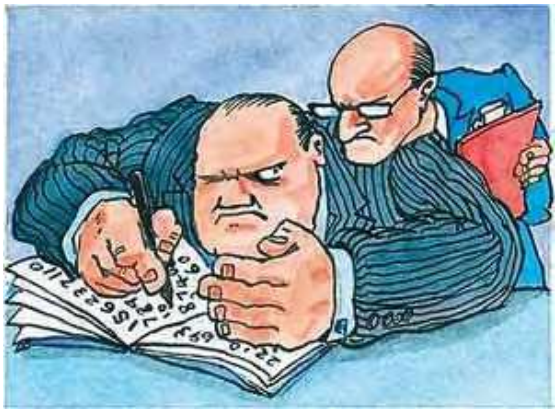
Accounting

Crooks and books

Jul 28th 2005
From The Economist print edition

How accounting reforms are creating problems as well as solving them



IT IS every boss's job to make his firm's profits look as good as possible. It is every regulator's job to keep this instinct in check. That's why accounting bodies the world over are pushing for reforms in the way companies keep their accounts. The thrust of the changes—to give a present, rather than an historical value for assets and liabilities—is broadly a good one, but it makes some sorts of scams (including a bit of what went on at Enron) easier. The reforms therefore need reforming.

Traditional accounting is based largely on static and objective but often irrelevant historic costs. Fair-value accounting, as the new system is called, updates items regularly in order to try to capture their current value. Last month America's Securities and Exchange Commission endorsed the shift to fair value; as a result, companies are likely to move faster towards this system (see article).

This is good news, for the most part, and should be supported. The goal of company accounts, after all, is to reflect economic reality as truthfully as possible. For some items, historic cost is clearly inadequate. Take, for instance, derivatives—options, swaps and the like. The latest figures from the Bank for International Settlements show that the gross market value of outstanding derivatives exceeds an eye-popping $9 trillion. Yet under historic-cost accounting, the rocketing growth of these instruments would not show up in company accounts because many derivatives cost nothing initially.

More transparency will help investors to make smarter decisions. Managers, too, are likely to do a better job. Accounting rules put in place in the early 1990s that forced firms to disclose health-care liabilities for retired workers, for example, drew salutary attention to the enormous obligations that corporate America was piling up. More recently, a new rule compelling firms to show employee stock options as a cost in their accounts has prompted many to rethink their pay policies.

Still, fair value does give rise to problems. For one, profits will be more volatile, because any change in a company's net balance-sheet position or income statement is taken into its profits-and-loss account. Critics argue that much of this volatility is “false”, reflecting market turbulence rather than a change in the underlying economics of the firm.

A second problem is that many items (bank loans, for example) are not traded on deep, liquid markets, and thus lack a verifiable price. Determining their “fair value” may involve complicated models based largely on subjective estimates. At best, these estimates are difficult for investors and auditors to verify or compare across companies. At worst, unscrupulous managers could manipulate models to flatter the bottom line, which is part of what happened at Enron.

Show your working

Both these problems would be mitigated by making firms disclose the assumptions behind their estimates, and how different assumptions would affect profits. They should also reveal whether estimated values had altered over time because market conditions had changed, the underlying business had changed, or they had made a bad guess the first time. Ideally, financial statements would also show, for key items, both the historical cost and the updated fair value, with an explanation of how to get from one to the other. Because companies already track this information, revealing it should not be costly.

More, and more useful, information would both help investors to decide whether estimates are fair or foolhardy, and encourage managers to value things realistically. It will also highlight the difficulty of measuring a firm's performance—a complex, subjective notion which cannot be captured in a single profit figure. If this prompts investors to think harder about what a business is worth, so much the better.

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Economist.com PRINT EDITION SPECIAL REPORT
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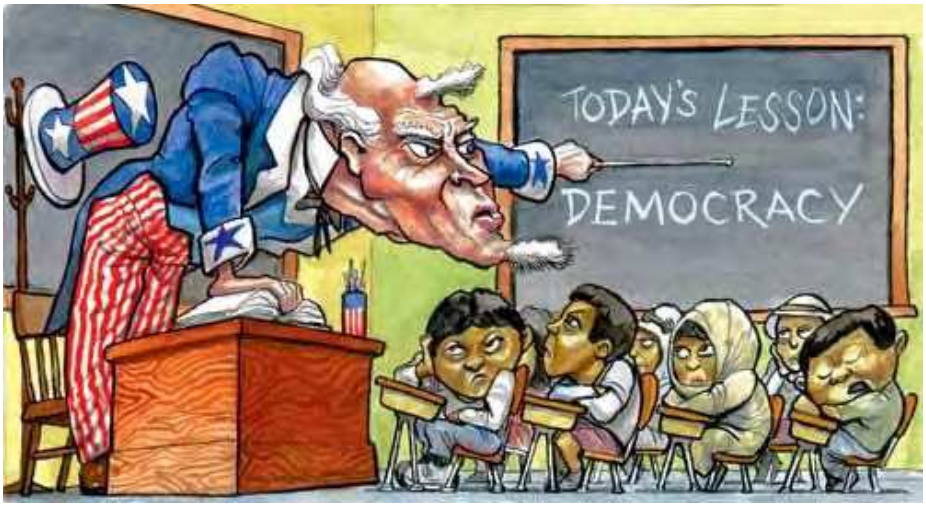
America and the Middle East

Does he know where it's leading?

Jul 28th 2005 | WASHINGTON, DC
From The Economist print edition



George Bush's administration has dramatically stirred things up in the Middle East. It's a high-risk policy pointing in many directions, hopeful as well as frightening

"DO WE turn right or left?" Such was the exuberant question—whether to press on to the north-east and chase the mullahs out of power in Tehran or head north-west and oust Bashar Assad from his dynastic throne in Damascus—on the lips of many of President George Bush's exultant neo-conservatives, as the marines burst through the gates of Baghdad in April two years ago.

Next came the no less exhilarating assertion of many neo-cons that "the road to Jerusalem goes through Baghdad", meaning that, once a pro-American democracy was entrenched in a grateful Iraq, the region's awed and admiring Arabs, Palestinians included, would be cajoled willy-nilly into an accommodation with Israel. Under the tutelage of the American hyperpower, peace, harmony and democracy would break out over the region.

It has not turned out that way. The Americans are bogged down in a bitter insurgency in Iraq which shows little sign of abating. All the roads that lead from Baghdad are booby-trapped. The regimes in Iran and Syria are refusing to collapse; indeed, the mullahs have just overseen the election of a president who sounds a lot nastier to the Great Satan than did his predecessor. Peace between Israelis and Palestinians is a bit closer than it was two years ago, but a lasting settlement looks as grindingly hard as ever to achieve. If opinion polls and anecdotal data are to be believed, the Americans are more disliked in the Arab world than ever before.

Worse still, the global terrorism that was one of the prime targets of the assault on Saddam Hussein's Iraq appears to have increased. Witness this month's rash of suicide bombings in Britain and Egypt (see article and article), the two countries with which America is most closely allied in Europe and the Middle East respectively. Indeed, it is widely assumed that the battle for Iraq has enlarged the pool of would-be Islamist terrorists keen to wreak anti-western havoc elsewhere.

And yet. Though the heyday of the neo-cons in Washington has passed, and those of their ilk still well-placed in the administration or cheerleading from outside it are less triumphal, Mr Bush is still undaunted in pursuit of the aims that have inspired them—and him—since he adopted his assertive new foreign policy in the wake of the attack on New York's twin towers in September 2001. "It's a long effort," says a senior administration official. "Things are still moving in a good direction...there's still a good deal of forward momentum."

In its defence, the administration habitually lists a string of achievements—and rosy events for which it can claim at least partial credit—to bolster Mr Bush's belief that "freedom is on the march". The successful election in Iraq in January is high on the list, though its sheen may have faded a little, as the insurgency refuses to die down. High, too, is the election of a more amenable Palestinian president, following the death of Yasser Arafat, and the resumption of a peace process with Israel under America's gaze. Lebanon's recent elections are much hailed too. Though it was Syria's miscalculation in (probably) assassinating a former Lebanese prime minister, Rafik Hariri, which led to Lebanon's "cedar revolution" and to Syria's humiliating withdrawal from its neighbour, the Americans argue, fairly, that it was their pressure that destabilised the regime, causing Mr Assad to overreach himself.

Bush is even badgering Pharaoh

There are numerous other instances of change in the region that probably would not have happened without America's assertiveness. Libya's Muammar Qaddafi has given up his weapons of mass destruction, for fear of sharing the fate of Mr Hussein. Last month Kuwait's first woman minister was sworn in, shortly after women had been given the right to vote. Bahrain is loosening up its politics. Earlier this year Saudi Arabia took its first tentative step towards representative government with elections to local councils.

Iraq apart, the most striking recent changes are in Egypt, long the most crucial of America's allies in the region but whose political and economic system had slipped into a sullen torpor under the deadening hand of Hosni Mubarak. In early September, for the first time in his 24-year-long presidency, he is to allow other candidates to compete for the top job in the Arab world's most populous country, 70m-strong. Though he fiercely denies giving in to American pressure and though an array of emergency laws, sure to be invoked after last week's bombings, still makes it hard for an opposition to compete on equal terms (he is all but certain to be re-elected), the political mood has nonetheless altered dramatically. America can certainly take the credit.

What has become plainer, in the past year or so, is that Mr Bush is utterly serious about trying to spread democracy across the region as a hoped-for long-term antidote to the cancer of terrorism which, in his view, is the product of undemocratic politics. He may, especially in the eyes of worldly European pragmatists, be naive in that belief. But he is not cynical.

Can they really dump their oldest pals?

Condoleezza Rice, the secretary of state, could not have made clearer, with her outspoken remarks at the American University in Cairo last month, her president's commitment to spreading democracy. "For 60 years, the United States pursued stability at the expense of democracy in this region here in the Middle East—and we achieved neither," she said. "Now we are taking a different course...supporting the democratic aspirations of all people."

> The day must come when the rule of law replaces emergency decrees—and when the independent judiciary replaces arbitrary justice. The Egyptian government must fulfil the promise it has made to its people—and to the entire world—by giving its citizens the freedom to choose. Egypt's elections, including the parliamentary elections [expected in November], must meet objective standards that define every free election. Opposition groups must be free to assemble and to participate and to speak to the media...And international election monitors and observers must have unrestricted access...

Phew. The neo-cons, with their determination to spread "American values" even at the risk of alienating undemocratic allies, were thrilled. "Removing Saddam Hussein has unleashed democratisation in the Middle East," said Bill Kristol, editor of Washington's *Weekly Standard*, the neo-cons' in-house journal. "Things are happening that would have been unthinkable a year or two ago."

Yet even the most irrepressible neo-conservatives know there are limits to what they and Mr Bush can try to do. What if democratic elections produce parliaments and governments that are even more hostile to America and the West than the despots who precede them? That, in the neo-con view, is a risk that has to be taken; Miss Rice has said as much herself. But what if America, impatient to put democracy before stability, risks losing any of its three key strategic allies in the region: Egypt, Saudi Arabia and Pakistan?

In Saudi Arabia, Mr Bush may step more warily than some of his neo-cons would like. They argue that America's past policy of benign co-operation did nothing to prevent the Saudis from producing 15 of the

19 hijackers who carried out the atrocities of September 11th 2001. Nor did it stop the Saudi authorities from letting Saudi clerics spread a gospel of hate among the credulous young. But, with Iraq in flames next door, Mr Bush may be loth to stir up more of a Wahhabi hornets' nest, despite his thirst for spreading democracy.

"Pakistan is the toughest call," says Mr Kristol, echoing the sentiment of many in the administration. Democrat or not (well, not), Pakistan's General Pervez Musharraf has done his best to bash al-Qaeda in his own country. But he has done a lot less, for fear of being overthrown, to root out anti-western preachers or to close hate-filled *madrassas* which spread their word abroad. So, even in the ideologues' wing of the White House, stability does occasionally trump democracy.

Another conundrum the administration now admits it cannot easily solve is whether groups it has deemed terrorists or otherwise unacceptable—Hamas in Palestine, Hizbullah in Lebanon, the Muslim Brothers in Egypt and elsewhere—should be lured, if possible, into the political mainstream, or isolated, or clobbered. Right now, it officially has nothing to do with any of them. If Hamas or Hizbullah intimates that it will cease violence and may even accept the notion of an Israeli state if most Palestinians do too, it may be hard for America to go on isolating them. "It's the Sinn Fein issue," says an adviser to Mr Bush's first administration. "My hunch is that we'll have to deal [peacefully] with [Hamas]...provided that it commits to non-violence and lives up to it."

And in two other areas, the administration is also staying its hand, despite its yearning for regime change: Iran and Syria. The much-touted phrase, coined by a neo-con, that "Syria is low-hanging fruit", ripe for plucking, is no longer thought apt. Besides, if Mr Assad's regime were to fall, there is a good chance that it would be succeeded by an Islamist regime even more hostile to Israel and America than Mr Assad's lot. So America's policy, meanwhile, is to let Mr Assad, already humiliated by his enforced retreat from Lebanon, stew in his own juice.

Leave those mullahs alone, for now?

For Mr Bush and his advisers, Iran is far more frustrating. The mullahs' regime has long been a top target of the neo-cons. Iran is the only country in the region that has not yet accepted that Israel should exist; it still sponsors Islamic Jihad, the most irreconcilable of Palestinian terrorist groups, and Hizbullah, the Lebanese Shia party-cum-militia that is moving into the mainstream of peaceful politics but has yet to disarm. Iran's secret drive, over the past two decades, to achieve a nuclear capability that could be turned to bomb-making, has rattled Europeans (who have been trying, so far in vain, to negotiate a bomb-stopping deal with the mullahs) as well as Americans of all political stripes.

A plan of action, of sorts

America's latest steps and hopes in the region

Bahrain	Hail gradual loosening of politics without demanding full democracy
Egypt	Prod Hosni Mubarak towards opening up politics; encourage democratic opposition but not, so far, the Muslim Brothers; risk annoying and undermining a strategic ally
Iran	Quietly admit that America is stymied for now; encourage democrats to undermine mullahs' regime; let Europeans try to stop it becoming nuclear-capable; muffle talk of regime change; fret at impossibility of taking tougher measures while Iran can make mayhem for America in Iraq but push for sending the nuclear file to the UN's Security Council
Iraq	Hope that new constitution will be agreed next month and that a referendum to endorse it, with greater Sunni participation, takes sting out of insurgents; build up Iraqi forces to enable American ones to draw down; hang in for a long haul
Israel	Reaffirm support; encourage Israel's withdrawal from Gaza strip; wait until it is over and for new elections among Palestinians and Israelis before re-engaging in a bigger way
Jordan	Encourage its benevolent monarch and his go-ahead wife towards modernity and controlled democracy
Kuwait	Hail slow loosening of politics and emergence of first woman minister without demanding full democracy
Lebanon	Hail the recent election, encourage the new government to freeze out Syria, hope against hope that liberal democracy emerges in a state still twitchy with sectarian tension
Libya	Hail its leader's disavowal of weapons of mass destruction, encourage American oil companies to go back in, fret mildly at continuing political repression
Morocco	Gently encourage a fairly benevolent monarch to continue to loosen up
Pakistan	Thank its leader for tackling al-Qaeda but nag him to curb radical *madrassas* and other Islamist groups while realising that he can't afford to
Palestine	Tell it to become a democracy and crack down on terrorists, with Gaza as a model; then help it to become a proper state in the West Bank as well, while letting Israel keep its biggest settlements there
Qatar	Hail steady loosening without demanding full democracy
Saudi Arabia	Welcome tentative steps towards limited representative government but nag away at the need for much deeper political and human-rights changes; risk enraging a strategic ally
Syria	Let it stew, punish it if it helps Iraqi or Palestinian insurgents, encourage secular dissidents, and hope that the regime will fall—with no idea what might follow

Turkey	Hail a good ally as a good example of how Muslims can elect a moderate Islamist government that can co-operate with America, join the EU, and continue to play a big part in NATO

Sources: *The Economist*

But, for the time being, the Americans are stumped—mainly because of next-door Iraq. The ultimate sanction against Iran—military strikes against a plethora of nuclear-suspect facilities, with or without Israel's help—would be operationally and diplomatically tricky, might set back the programmes by only a few years and, worst of all, would prompt Iran to make even more mayhem in Iraq than there is already. Many neo-cons still insist that the regime in Tehran is ripe for removal and that America should do more to help democrats there. But rapid regime change has dropped way down the agenda.

Top of the agenda

For the American administration, today's two biggest issues in the region, by far, are Iraq and Israel-Palestine—in that order. Despite the age-old urgings of Europeans and Arabs that a solution to the Israel-Palestine puzzle would give a huge boost to the West as a whole in its war against Islamist terrorism, it comes far below Iraq on Mr Bush's list of things to worry about.

In a nutshell, America wants “Gaza to work” first; moving on to negotiations for a final settlement depends on many other things happening. Virtually all Mr Bush's Middle East advisers criticise Bill Clinton for getting “too involved” in the day-to-day management of the Israel-Palestine issue. And the administration fiercely rejects the notion that the plight of the Palestinians is a prime cause of instability throughout the Middle East. Indeed, Ms Rice has scolded Arab leaders for using the issue as a shield behind which to hide their own defects.

America's first hope is that the secular-minded Fatah movement of Palestine's president, Mahmoud Abbas (aka Abu Mazen), will re-assert its authority in Gaza and the West Bank—and win a parliamentary election now due in January; it was put off this month for fear that the Islamists of Hamas would win. At present, Israel and America refuse to deal directly with Hamas—even though it has recently won the mayoralties of a number of Gazan and West Bank towns and probably commands a third or more of the Palestinian national vote—because, though it has more or less abided by a ceasefire brokered earlier this year, it has not disavowed violence and still refuses to recognise Israel. Instead, the American administration hopes that, once the Israeli settlers have been evacuated from Gaza by early September, Mr Abbas's Palestinian government will begin to build up its popularity by making life better for the miserable Palestinian people, squelch violence, then present itself as a credible interlocutor with the Israelis in the next stage of negotiations: to create a Palestinian state within provisional boundaries on the rest of the territory (or on most of the rest of it) occupied by Israel since the 1967 war.

At this point, the American administration is a bit vague, as indeed, studiously, is Ariel Sharon, Israel's prime minister. Both are wary of getting into discussions, at this stage, about the final shape or size of a Palestinian state on the West Bank, though Mr Bush says it must be contiguous, sovereign and viable—and has commented rudely on the route of the barrier that “snakes” (his word) through chunks of Palestinian land, including parts of Jerusalem.

In any case, say the Americans, even if Gaza “goes well”, it is uncertain who will be running the Israeli show next year. Mr Sharon still has to quell opposition within his Likud party. Israel's Labour Party, now in the ruling coalition, will also be choosing a leader. A general election in Israel must happen by November next year—and may be held as early as February. After the Palestinians' expected general election, their leadership could change too. Meanwhile, say the Americans, let's see what happens in Gaza.

It is Iraq that commands much greater attention. It is widely believed by Mr Bush's friends in Washington that his entire presidency will now be judged on the outcome there. “If Bush fails in Iraq, he's a failed president,” says a prominent neo-con pundit. Here, again, the Bush team remains doggedly optimistic. “Compared with where we were in January, we're light years ahead,” says a Bush appointee in the State Department.

The immediate hope is that a new constitution will be agreed to, ahead of time, in the next week or so; that a visible Sunni imprint on it will inspire a lot more Sunnis to turn out for a referendum in October than they did for the election in January; that the Iraqi security forces will gradually be able to stand on their own feet, allowing the Americans to start drawing down their forces within a year or so, and that, slowly, the insurgents will be contained.

At that point, of course, Arabs elsewhere will look enviously at the region's first federal democracy—and will no doubt wish to emulate it. So far, however, even among the most loyal of optimists in the White House, there is a sense that a “tipping point” in favour of the new order may not occur until Mr Bush's presidency is over. If Iraq is then still in a mess, a new (Democratic?) president might well cut and run—leaving America's image in the region in tatters.

Where does that leave America's campaign to democratise the region? There is no doubt that its promotion of the democracy ideal has stirred up a healthy debate and given Arab democrats fresh hope—though very few think it wise, yet, to thank America for it. Outspoken liberals such as the Lebanese-American, Fouad Ajami, who wholeheartedly applauds the policy, are in a small minority, at least among Arabs prepared to go public. And opinion polls among Arabs—for example, one conducted last year by Zogby International and the University of Maryland—show sky-high levels of cynicism, especially in countries such as Jordan and Saudi Arabia whose governments are friendly to America, about American motives in the Middle East. By overwhelming margins, Arabs think “oil” and “Israel”, not a desire to promote democracy, drive American policy in the region. Polls also suggest, by huge margins, that Arabs do care passionately about Palestine—and that helping to create a viable Palestinian state would vastly further America's cause.

Thank you, one day, perhaps

What is undoubtedly true is that bringing democracy to the region is a long-term, even generational, project. Elections are one thing; slowly building civil institutions and fairer legal systems, inculcating a culture of tolerance and debate, finding a new balance between clerical and secular authority, giving women a voice—is quite another, and takes much longer.

Meanwhile, at any rate to begin with, America is sure to remain deeply unloved. The question is whether, over time, Arabs will be grateful to it for starting a process, however clumsily, which may—just may—lead to good in the end.

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Northern Ireland

I Renounce Arms

Jul 28th 2005
From The Economist print edition

PA

The armed struggle is over, but the political struggle goes on

Get article background

FOR a group that has survived on ambiguity and twisted words, the declaration was unusually clear. On July 28th, after months of bickering and delay, the IRA pledged to “end the armed campaign” in a statement designed to signal that the terrorists had put more than three decades of bombing and shooting behind them once and for all. Only the IRA's history of reluctant and glacial change diminished the sense that, this time, Northern Ireland might at last be promised peace.

The statement marked the moment in Irish republicanism when Sinn Fein, once scruffy political cover for the terrorist operation, became the movement's centre of power. “All IRA units have been ordered to dump arms,” it declared. “Volunteers” were ordered to work towards “purely political and democratic programmes through exclusively peaceful means...We believe there is now an alternative way...to end British rule in our country.” To an old Provo worth his Armalite, such language would have amounted to apostasy. The IRA might continue to exist, but as a husk—an association of old comrades.

As if to underline Sinn Fein's ascendancy, the statement was presented by the party's leaders in the world's capital cities: Gerry Adams, the party's president, was in Dublin and Martin McGuinness, its chief negotiator, in Washington, DC. Even the timing of the announcement captured something of the shift from violence to politics: by all accounts, it had been delayed because the republicans did not want news of their statement to be overshadowed by the new, more violent terror campaign being waged by *jihadis* on the British mainland.

Mr Adams and Mr McGuinness, more than anyone, have over the past 12 years patiently coaxed the IRA towards this moment. Mr Adams first hinted at Thursday's move in April, when he publicly asked the IRA for ideas on how to achieve its aims by “purely political and democratic activity”.

The Shankill shuffle

For many years Britain and Ireland had feared that the embrace of politics would inevitably lead to a violent and bloody republican split. But, frustrating as they were, the years of doublespeak and argument have served one purpose: as the supporters of violence have been talked round, the power of the extremists has gradually withered. Few republicans these days expect a backlash.

Instead, they are awaiting their reward from the British and Irish governments. Tony Blair immediately praised the IRA's pledge, pointing to its “clarity” and “the recognition that the only route to political change lies in exclusively peaceful and democratic means”. He will now be expected to allow the removal of watchtowers in South Armagh, along the border with the republic, and the free return to the North of “on the runs” (suspected or absconded IRA members wanted for questioning). After a suitable period of IRA inactivity, the Irish prime minister, Bertie Ahern, may indicate that Sinn Fein will be eligible as a possible coalition partner in future Irish governments.

The doubts lie with unionist politicians who equate Sinn Fein with the IRA. Jeffrey Donaldson, a leading member of the hardline Democratic Unionist Party, threw cold water on the statement, asking: “How do we know that the IRA is not going to continue criminal activities?” Besides, he demanded, when would the IRA disarm? He may well get an answer sooner than he expected: there is talk that the IRA may decommission its arms—witnessed by international monitors and priests from the Protestant and Catholic churches—as soon as this weekend.

Many in and out of the unionist movement worry that, even if the IRA renounces political violence, its links with crime will persist. The statement sought to banish that concern, saying its members “must not engage in any other activities whatsoever”. It remains to be seen whether there will be more raids on Belfast banks or casual murders outside pubs.

If all goes well—still a very big if—Northern Ireland could see elections and, by next autumn, a new government containing unionists and republicans. There is so much to argue over before then, about who is suitable to govern, about the control of the police, about who does what. But that, after all, is what normal politics is all about.

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Shooting to kill

Excuse me, are you a suicide-bomber?

Jul 28th 2005
From The Economist print edition

The public support the police over the killing of an innocent man

LAST Friday morning Jean Charles de Menezes, a 27-year-old electrician from Brazil, walked out of a block of flats in south London. He took a bus to the Tube, perhaps a little late for work. When he ran on to a train he was pinned to the floor of the carriage by men in plain clothes who fired eight shots at close range—seven to the head and one to the shoulder.

From the police's point of view, the story is rather different. They were watching Mr de Menezes's building because they thought it was linked to a bomb attack on London on July 21st. They saw someone leave of a similar age to the wanted men. He was wearing a warm coat on a hot day. At the Tube station, they identified themselves and challenged him. He ran on to a train. Fearing he might have a bomb beneath his coat, they fired.

Shootings by the police, very few of whom routinely carry guns, are rare in Britain—there are about two or three in a typical year. That is one reason why Mr de Menezes's death is shocking. The other is that most police shootings do not take place at point blank range and in crowded public places. Some Londoners have now started to worry that there is a new shoot-to-kill policy in place on the Underground, to add to the fear of bombs.

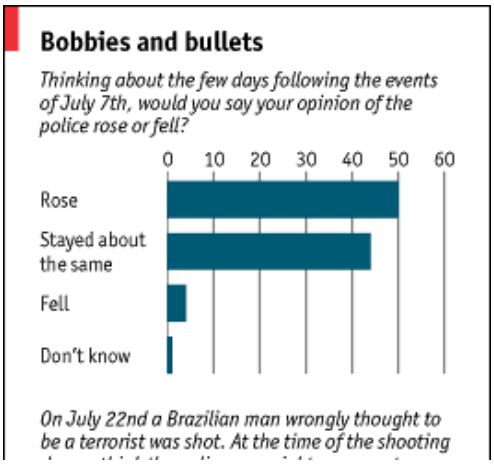
In fact, police policy has not greatly changed: guidelines have long said that officers should shoot to incapacitate the threat. Police marksmen usually aim for the torso because it is the largest target, rather than out of compassion.

What has changed are the conditions in which the police now have to choose whether or not to pull the trigger. If someone has explosives strapped around his belly, then incapacitating him means shooting to the head. Challenging a suicide-bomber to stop may act as an invitation to trigger a bomb, so the police may feel that they should shoot first. Whatever they decide to do, they must do quickly.

All of which amounts to a big test for the police. So far things are going surprisingly well—at least as measured by public opinion. Because shootings are infrequent, the public trusts that the police are not trigger-happy and assumes that they make the right decision when they kill.

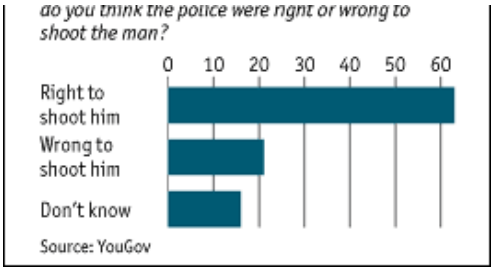
A poll by YouGov for *The Economist* found that the public believes the police were right to shoot Mr de Menezes at the time even though the intelligence on which they based their decision turns out to have been faulty (see chart). An independent inquiry has been set up to look at what went wrong. But most people support the shoot-to-kill policy and more than a third favour even tighter policing.

One possible reason for public confidence is that the police investigation has moved quickly. Images of the bombers were released on July 22nd, a day after the attack. Two of them were later named as Muktar Said Ibrahim and Yasin Hassan Omar. What appeared to be explosives were found at Mr Omar's home in north London. Police made a large number of arrests in London and Birmingham. One man, incapacitated with a Taser gun, was thought to have been among the bombers.


Bobbies and bullets
Thinking about the few days following the events of July 7th, would you say your opinion of the police rose or fell?
0
10
20
30
40
50
60
Rose
Stayed about the same
Fell
Don't know
On July 22nd a Brazilian man wrongly thought to be a terrorist was shot. At the time of the shooting

The investigation has uncovered intriguing differences between the men who tried to detonate bombs on July 21st and those who killed 52 people two weeks earlier. The bombers who struck on July 21st picked less promising targets: one planted a bomb on a bus that was virtually empty. While the first group was composed of respectable-seeming black and Asian Britons, the second

appears to have included at least two refugees from East Africa, one of whom has a criminal record. Police are now searching for a man, or men, who may have co-ordinated both terror groups.



Sir Ian Blair, the head of London's police, is confident enough that his officers will catch the bombers to have prepared the public for further embarrassing mistakes. But further shootings will make Muslims jumpier, at a time when police badly need their help. It may also prove a problem for the armed part of the force, whom the public trusts at least in part because most of their bullets stay in their magazines. Rather like the terrorist attacks themselves, the first shooting of an innocent man is a tragedy, but a second would look like part of a pattern.

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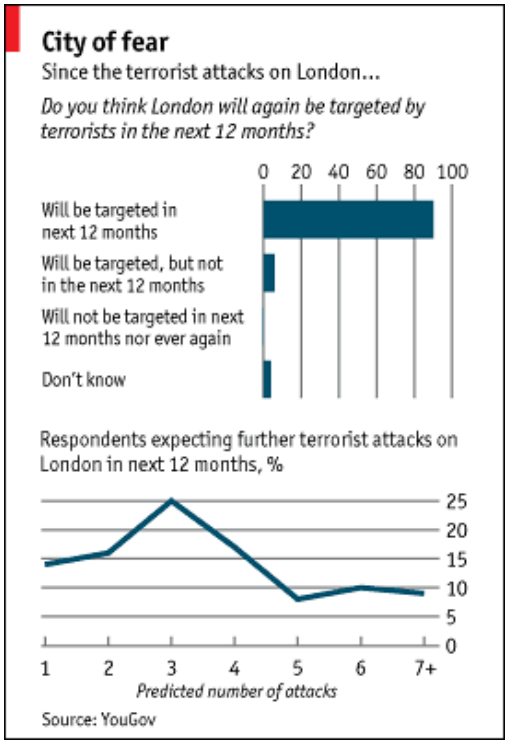
Terrorism

Learning to live with it

Jul 28th 2005
From The Economist print edition

The bombings will change London, but not in the ways most people expect


City of fear
Since the terrorist attacks on London...
Do you think London will again be targeted by terrorists in the next 12 months?
0 20 40 60 80 100
Will be targeted in next 12 months
Will be targeted, but not in the next 12 months
Will not be targeted in next 12 months nor ever again
Don't know
Respondents expecting further terrorist attacks on London in next 12 months, %
25
20
15
10
5
0
1 2 3 4 5 6 7+
Predicted number of attacks
Source: YouGov

"OUR lucky day" was the judgment of one British newspaper on the second attempt in as many weeks to murder users of London's transport system. Unlike the four men who blew themselves up on July 7th, killing 52 others, the plotters who struck a fortnight later failed to take lives. But the second bombing hinted, unnervingly, at a long-term campaign. Before July 21st, London was recovering from a past atrocity. Since then, it has been coping with an enduring menace. Two terrorist bombings, it turns out, are more than twice as bad as one.

If spreading fear was the terrorists' objective, they have succeeded. A poll for *The Economist* shows that 90% of Britons (and almost the same share of Londoners) believe the city will be targeted again within a year. Fully 59% reckon that travelling in the capital has become more dangerous, while only 1% believe the opposite.

But what will be the lasting effect of the bombings? There is a simple rule of thumb. If it is difficult to imagine something ever returning to normal, it is likely to do so quickly. The sources of long-term disruption and damage are more subtle. Much of the harm will come only indirectly from the attacks, and will be caused by the responses to terror rather than the terror itself.

Any fear and anxiety whipped up by the bombings will dissipate quickly. "Most people recover of their own accord in just a few weeks," says Anne Eyre, a consultant who specialises in trauma and disaster management. While some people who were close to the bombings or have experience of traumatic events will find it harder to recover, the great majority will not require counselling or therapy.

That was so even in New York, where the attacks of September 11th were far more deadly and visible

than the London bombings. Project Liberty, a federally funded outfit, deployed thousands of counsellors to meet some 1.2m people. Just 6% were referred for further treatment, mostly for minor symptoms such as sleeplessness. Another survey found that the share of local people reporting symptoms of trauma fell by two-thirds in the six months following the attacks.

Travelling habits will return to normal just as quickly. Andrew Evans, of the transport research unit at Imperial College, says people often declare they will never return to a network that has suffered a calamity. But most soon do so. The exception is the King's Cross fire of 1987, which killed 31 people and led to revelations about the dangers of the Tube that were as shocking as those exposed in the past few weeks. Even then, passenger numbers fell below expectations by just 6% in the first year and returned to normal within three years. Some of that was probably due to fears of nothing more scary than a delay.

One measure of Londoners' jumpiness is how often stations and lines are closed following reports of something suspicious. In normal times this happens twice every three days. In the week after the July 7th atrocities, when every bag seemed to contain a bomb, there were an average of ten closures a day. In the following week, though, this number fell to just under four, before increasing again after the second wave of attacks. That suggests only frequent atrocities will cause havoc.

City workers are even steelier. The FTSE 100 share index wobbled slightly on July 7th, losing 4% of its value before recovering later in the day. Such calmness is to be expected. Rafi Melnick, who follows the Tel Aviv stock market at the Interdisciplinary Centre in Herzliya, says that bombings affect equity values only if a campaign is prolonged and deadly. World markets reverted to trend (a downward one, as it happened) within two months of the September 11th attacks, which struck the financial sector directly.

A corporate exodus to Frankfurt or other cities is also unlikely, in part thanks to London's pre-eminence in finance, in part because of the cumulative effect of attacks. As the tally of cities struck by Islamist terror lengthens, every financial centre begins to look like a potential target—which means none seems especially risky.

Other big industries such as tourism and retail will suffer more, at least in the short term. Oxford Economic Forecasting, a consultancy, estimates that Britain's tourism industry will lose about 1.5m visitors by the end of 2006. That does not take into account the second bombing. The London Chamber of Commerce and Industry believes the failed attack, which has been widely reported outside Britain, will displace more tourists and shoppers, although the shoppers will probably go only as far as the suburbs.

Of all the shocks caused by the bombings, none will endure as long as the measures that are put into place to stop them. Terrorism jolts most people, but a few react by calmly seizing the opportunity to push long-nurtured demands. The notoriously militant RMT transport workers' union moved quickly, insisting that plans to reduce station staff be put on hold and extra guards be added to trains.

The Association of Chief Police Officers, representing senior coppers, tabled no fewer than 28 suggestions for reform. These range from extending the maximum holding period for suspected terrorists from 14 days to three months (which the government seems to favour) to more powerful and wide-ranging search warrants and—no surprise, this—more money.

Such a flurry of opportunistic demands, when presented to a government that is keen to “do something” about terrorism, can result in colossal distortions to spending. In America, the Department of Homeland Security burns through almost $40 billion a year, routinely doling out grants to places that are unlikely to be on any terrorist's target list. For that reason, it may be lucky that MPs have already quit Westminster for their villas and rural retreats. Work on a promised anti-terrorism bill will resume only in October.

Meanwhile, the police carry on. Their conduct over the next few months poses the greatest long-term threat, as well as the best hope for stopping further attacks. So far, London's Metropolitan Police have a mixed record. Mosques have been visited and politically incorrect talk avoided. But the shooting of a man mistakenly thought to be a terrorist (see article) has set some Muslim nerves on edge.

The danger is that Muslims'relations with the police will sour, rather as happened with Afro-Caribbean men in the 1980s. Black anger stemmed from the seemingly prejudiced use of street searches—a tactic that, ominously, was increasingly directed against Asians even before the London bombings. Between 2000-01 and 2003-04, the number of Asians stopped and searched rose by 60%, compared with an 8% rise among the population of England and Wales. Fewer of these searches led to an arrest than searches of any other ethnic group.

In the aftermath of terrorist attacks, the extravagant use of such police powers might seem tolerable, or even desirable. In the long term, the consequences are more likely to prove otherwise.

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MG Rover

Rover's return

Jul 28th 2005
From The Economist print edition

At last a buyer—but romantic talk of a revival is far-fetched

THE British Government couldn't save it and neither could BMW's £4 billion, but now the Chinese Government wants to have a go at rescuing MG Rover.

Nanjing Automobile—founded in 1947, loss-making and the oldest vehicle-maker in China—has outbid its rival Shanghai Automotive Industrial Corporation (SAIC). Both are state-owned.

It is a little early in China's participation in the global car industry to be making overseas acquisitions. The Japanese never did and South Korea still hasn't, despite having winnowed its industry to one dominant manufacturer.

Rover no longer really matters to the British motor industry. Thanks to investments by Ford, General Motors (GM), Peugeot, Toyota, Nissan, Honda and BMW, and the preservation of Land Rover, Jaguar and Mini, Britain is building 1.6m cars a year. Rover was down to 120,000 and falling fast—fewer than the number of Minis built each year by BMW in Britain.

Despite the formal declaration on July 21st of a winning bidder by PricewaterhouseCoopers, the administrator, Nanjing must overcome several obstacles before it can restart making MG saloons and sports cars. SAIC is unhappy that its bid was worth more in total than its compatriot's £50m and may yet launch a formal protest. And a consortium headed by David James, himself an administrator who sorted out the Millennium Dome, also wants a hearing for its competing bid. They might as well now talk direct to Nanjing. No sooner was it declared winner than it was out and about trying to sell the bits it hadn't really wanted in the first place.

Why would two Chinese companies both want Rover? There are 26 Chinese vehicle-makers, from Anhui to Zhongxing, and 19 foreign ones. Annual production has reached 4m and is growing at a rate that is unprecedented in other developing economies. But despite the Chinese government inviting all and sundry to build cars in China, the indigenous carmakers still have little proprietary technology of their own.

Under the deals struck with the Chinese authorities over the years, western and Japanese carmakers have had to find a local partner to help with manufacturing. Thus SAIC builds Volkswagens and GM cars in China, while Nanjing, with annual production of 200,000, is heavily involved with Fiat, another troubled European carmaker. But the Chinese carmakers do not have a good grip on vehicle research, components technology, purchasing or brand-building. All they really understand is vehicle assembly.

That is why Rover's know-how is so attractive. It has a design centre that is bang up to date—despite the dwindling income to sustain it—and a reservoir of experience going back to the time when it was part of the world's fourth-largest motor group.

Rover's receiver may be past caring if its intellectual property is nicked. Survival is the main aim of a business whose assets are worth little and whose creditors want £1.4 billion. But former partners will care. Honda was the creator of Rover's 45 model many years ago and has already been in to see the receiver to recover blueprints and copyrights. BMW built the Rover 75 and could yet take a similar stance. No doubt Nanjing will be delighted to have a peep at the files relating to these two remarkably successful carmakers.

What Nanjing will be less happy about as time passes is its liability to renew the cars in the MG range (SAIC claims to have paid for the rights to the Rover brand name). Between them, the 45 without Honda's help, the 75 without BMW and the MG mid-engined sports car without anybody probably call for an investment programme costing £2.5 billion.

That is why, for all the talk, the chances are that Nanjing will continue to shrink Rover—something that has been going on since the merger of Leyland and British Motor Holdings in 1968. What Rover knows about car-making will be transferred back home to China—but by the time it gets there, Nanjing's foreign rivals will already be on to the next big thing.

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Social conservatism

Meanwhile, back in the shires

Jul 28th 2005
From The Economist print edition

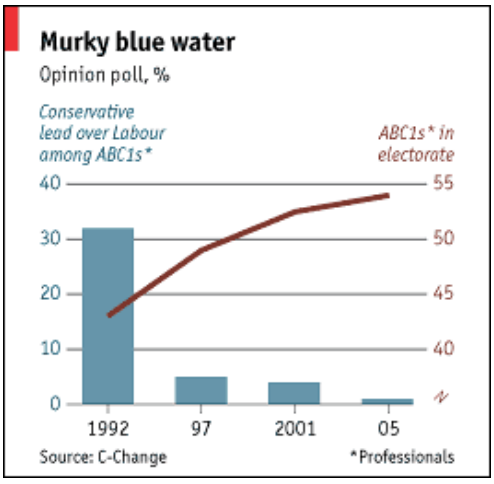
Why embracing social conservatism will not help the Tories

EVER since Michael Howard said he was standing down as leader of the Conservative Party, the front-runners to replace him have been playing a strange game. The candidates have tried to explain why the Tories have been in the doldrums since 1997, agreed that the party must sound more idealistic and less uncomfortable with Britain today, and then each proposed a different miracle formula for victory, containing some combination of tax cuts and reformed public services. This entertainment has not been dull exactly, but it has been jolly sensible. A nutty new prescription for success from some socially conservative Tories is thus welcome.

The Cornerstone group, a flock of about 25 MPs, says its votes are there to be won by the candidate who shows most sympathy with its way of thinking. This being the Tory party, that unity might not hold. But they make an interesting group, combining high Tories such as Edward Leigh with pavement-pounders like Andrew Rosindell, MP for Romford. Mr Leigh is a Catholic Eurosceptic who is also the somewhat ineffective chairman of the Public Accounts Committee in the House of Commons. This week he gave a good indication of Cornerstone's likes and dislikes, when he published a pamphlet outlining a Conservative alternative to the liberalism that he says “has managed to infect the Conservative Party like a virus”. Tories, he declares, should stop “shillying and shallying around” and stand on a platform of faith, flag and family. It worked for George Bush, so why not try it in Britain?

There are at least three reasons why not. First, Mr Leigh's conservatism is in fact very different from Mr Bush's. America's 43rd president is forward-looking and optimistic, and therefore attractive to young voters and immigrants. Mr Leigh, by contrast, takes his ideas from a fustier strain. Like the character in Evelyn Waugh's “Vile Bodies” who looks out of an aeroplane window at the new suburbs and is overcome by nausea, Mr Leigh thinks that “no conservative can look at the soulless ubiquity of our town and city centres or the dreadful and capricious power of supermarkets with anything other than horror”. This sort of thing irritates most Britons (frequent patrons of those satanic marts) and is a real turn-off for young voters and immigrants, who were not there to appreciate how wonderful things used to be.

Second, Britain is too socially liberal to show much enthusiasm for policies overtly based around supporting marriage (the family bit). Polling commissioned recently by Lord Ashcroft, a former Tory party treasurer, showed 66% agreeing that “it is not a matter for political parties to express a preference between two-parent and one-parent families.” Worse, the most liberal attitudes are to be found among professionals, who have been deserting the Tories even as their share of the vote rises (see chart).



Third, Britain lacks the well-attended churches with their politically active congregations that are the engine of American conservatism. Mr Leigh points to data from the 2001 census, when 72% of people described themselves as Christian, and argues that this is a constituency in search of a party. But the census question was not compulsory and threw up some odd results: nearly 400,000 people said their religion was Jedi. Church attendance is a better guide to faith in Britain, and only 4m people go every week. A brave attempt from Mr Leigh, then, but not enough to get the Tories very far.

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Financing the Tube

Underground underwater

Jul 28th 2005
From The Economist print edition

Not all is well with the part-privatisation of the London Underground. Unfortunately, Londoners are stuck with it

Get article background

THE public-private partnership (PPP) on London's Underground, under which responsibility for the rails, stations and trains was contracted out to the private sector, has been controversial ever since it was first suggested in 1997. The scheme has now been running for two years, but the criticism shows no signs of abating.

The National Audit Office, a respected watchdog, has attacked the project on value-for-money grounds. The House of Commons Transport Select Committee published a scathing report in March. In April Bob Kiley, the boss of Transport for London (TfL) and a vocal opponent of the scheme, said that performance on parts of the network was “bordering on disaster”.

All that calls for close scrutiny of the latest report on the scheme, from TfL. The government body responsible for transport in the capital quite reasonably concluded in its first report, published a year ago, that it was too early to tell whether the scheme was working or not. Its second report, published on July 27th, is much more forthright.

In some areas Metronet and Tube Lines—the private consortiums or “infracos” which manage the infrastructure—are doing rather well. Train reliability has improved on most lines. That's good news: faulty trains are a big cause of delays on the network, and so these are better, too. Passenger numbers are up. Staff are friendlier, and turn up to work more often.

But in other areas there are big problems. Much of the renewal work (refurbishing or replacing rails, lifts, stations and so forth) is running late. Signals still break down frequently. Engineering works, which take place at night or over weekends, often finish late, and the over-runs are getting worse—up 35% on last year. That means more delays for passengers in the morning rush-hour. None of this, says TfL, bodes well for the big infrastructure upgrades due to start in the next few years. “In short,” says the report, “performance is not good enough and is less than what was promised”—criticism the infracos reject as unfair.

Metronet, which manages two of the three infrastructure contracts, is singled out for special criticism. Its plans to replace rolling-stock on one line are already a year behind schedule, and work on refurbishing stations and track is delayed.

In theory, a mind-bogglingly complicated system of targets, rewards and fines should align the interests of infracos and passengers. Yet missing targets has not stopped Tube Lines and Metronet making healthy profits, of £42m and £51m respectively. Many experts see this as evidence that the companies have done much better out of the contracts than taxpayers have. “This shows that the public sector just doesn't know how to write very good contracts,” says Tony Travers, of the London School of Economics. Partly that's because of a lack of specialist knowledge, but politics has also played a part. “Both firms knew that the government was committed to this,” says Mr Travers. “That will have allowed them to get very good deals.”

How can things be improved? It is interesting to compare the tube with Britain's national railways, where Network Rail, the company that owns the infrastructure, brought maintenance back in-house a year ago. Cost savings already amount to around £100m, with more to come, and, without complicated contracts getting in the way, things are running much more smoothly. Geoff Pope, a Liberal Democrat and a member of the London Assembly, a political watchdog, wants the same thing to be done with the Tube.

That's probably impossible. The PPP contracts run for 30 years, and pulling out would mean paying hundreds of millions of pounds in compensation. Tweaking the incentives might help, but that would mean renegotiating the contracts. Legally, that cannot be done for another five years.

Of course, the PPP is as much a political invention as a legal one and in politics there is always a certain room for manoeuvre. If a new idea (such as closing lines for a few weeks to do maintenance, rather than trying to shoehorn it into evenings and weekends) is to both sides' advantage then new arrangements might be possible. The government can also wield other sticks: London is to host the Olympic Games in 2012 and there will be an almighty row if foot-dragging by the infracos leaves the Tube unable to cope.

But unless things get very bad indeed, Londoners look like being stuck with the existing deal, at least for the foreseeable future. The phrase most frequently heard from people connected with the project is “we are where we are.” The only thing left is to make the best of it.

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Bagehot

The summertime blues

Jul 28th 2005
From The Economist print edition

The spectacular restoration of Tony Blair's fortunes has left problems for everyone else

THE mood of MPs leaving Westminster for their summer break is troubled and uncertain. It's partly the possibility of a new terror attack and an early recall of Parliament. But there's something else: a kind of collective post-election depression.

On the face of it, Labour MPs have least to complain about. The gloom that accompanied the savaging of the government's majority quickly evaporated, as did the chorus of calls for Tony Blair to quit. But while the transformation in the prime minister's fortunes over the past two months should ensure that he and nobody else will decide the moment of his departure, the rejoicing on the Labour benches is muted.

It is simplistic to blame the unease on disgruntled Brownites—they are not too unhappily resigned to Mr Blair carrying on for at least two more years. Even they feel grudging admiration for the prime minister's recent performance. But Labour MPs are acutely conscious that Mr Blair's new Sun King status is neither as secure as it seems nor, even if it lasts, an unmitigated blessing.

The public's response to further terrorist atrocities is unpredictable. A Populus poll in the *Times* this week came up with the paradoxical finding that although nearly two-thirds of voters think Mr Blair's Iraq policy has made them less safe, his personal standing has rarely been higher. Moreover, a growing number of Labour supporters now wish he would reconsider his promise to stand down before the next election.

At his monthly press conference this week, Mr Blair made a passionate defence of his actions since the attacks of September 11th. He believes that instead of seeing Iraq's torment as proof of his and George Bush's folly, people can now see the connection between the indiscriminate murder of Iraqi school children, the attack on Sharm el-Sheikh and the bombing of the Tube. In other words, Mr Blair accepts a linkage between terror in Iraq and London, but only in the sense that both are manifestations of the same wicked ideology that must be confronted and defeated.

However, even if Mr Blair wins that argument—still an uncomfortably big if—he will remain vulnerable. If the terrorists show themselves capable of causing mayhem on a regular basis, the feeling could grow that the state was failing in its most fundamental duty: to protect the lives of its citizens.

To these fears are added more prosaic concerns. Inevitably, the present crisis has encouraged the prime minister's instinct for detaching himself from the fray of party politics. That's all very well for now, say Labour MPs, but in four years' time, they will depend on Gordon Brown, not Mr Blair, to save their seats. The praise lavished on Mr Blair over the past few weeks has come at a price for the chancellor, who suffers by comparison.

Finally, there is some anxiety that if the terrorist threat absorbs too much of the prime ministerial attention span, the domestic agenda, especially the hard grind of forcing change through the health service and the school system, will be neglected. Mr Blair is aware of the risk, which, he predictably claims, is one more of perception than of reality. But it is always hard to deal with more than one big thing at a time.

The other parties must wish they had such problems. Even among Tory MPs, there is a feeling that the protracted leadership contest is remote from anything that at the moment seems important. Although they are now united in condemning the hopelessness (in both senses of the word) of Michael Howard's election campaign and although the more perceptive among them understand how little the party's plight has been changed by winning back a few seats, there is no agreement on what to do about it.

The two front-runners, David Davis and David Cameron, could hardly see things more differently. Mr

Davis thinks the answer lies in rediscovering Thatcherite verities; Mr Cameron advocates a Tory version of Blairism. A devastating analysis of the Tories' predicament published this week by Policy Exchange, a think-tank, should bolster Mr Cameron's cause.

One of its findings was that, while 52% of voters could identify with the values of both Labour and the Lib Dems, only 34% shared values with the Tories. Policy Exchange also shows how unlikely it is that the Tories can win the next election. They came third in more seats than ever, they have become irrelevant in Britain's cities (outside London) and their core vote is shrinking. If Tory MPs realise they should be electing a leader for the long-haul, Mr Cameron's youth, seen by some as a disqualification, may actually be an advantage.

Tone alone

At least the Tories will soon have a new leader in whom to invest new hope (for a short while, in any case). The frustration for Liberal Democrat MPs is that they are stuck with a leader, Charles Kennedy, in whom they no longer have much confidence. The election, despite the handful of seats they gained, is now seen as a missed opportunity.

The doubts about Mr Kennedy's leadership that arose last year have resurfaced. The most serious is that Mr Kennedy has neither the intellectual energy nor the strategic grip to give his party the clear direction it needs. One senior Lib Dem admitted after the election that the only thing binding together the party's policies was the document they were in. Senior MPs accuse Mr Kennedy's fiercely protective kitchen cabinet of shielding him from criticism. But as long as the maverick Simon Hughes is seen as Mr Kennedy's strongest challenger, he is probably safe.

As Mr Blair packs his bags for his ninth summer holiday since becoming prime minister, he is more than ever the pole around which British politics revolves. Everybody is asking what it will be like when he's gone. But it is hard to imagine. Mr Blair, bombs permitting, will enjoy his break. Few others from the Westminster village will be so relaxed.

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Vacancy

Jul 28th 2005
From The Economist print edition

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French politics

The surprising Dominique de Villepin

Jul 28th 2005 | PARIS
From The Economist print edition

AP

A prime minister who is doing better than many had expected

Get article background

WHEN Dominique de Villepin was appointed France's prime minister on May 31st, the choice was widely considered eccentric, to say the least. A sour anti-elite mood had just led French voters to reject the European Union constitution in a referendum. President Jacques Chirac responded by picking an unelected aristocrat. The French were feeling glum about unemployment and globalisation. Mr de Villepin, a poet, has never held an economic portfolio in his life. Yet, two months on, France's new prime minister seems to be working out rather better than his critics predicted.

To glimpse the man the French thought they were in for, consider a random passage from one of Mr de Villepin's (many) recent books: “Today orphaned, faltering, easily disillusioned, France still burns with a desire for history: she has kept intact the flame of a great nation, fervent defender of her status.” Famous for his rousing defence, as foreign minister, of France's objections to the war in Iraq, Mr de Villepin was known for his romanticism and impulsiveness, his poetry and his history books, his admiration for Napoleon and his idealisation of the state. “Everyday matters bore him, mediocrity depresses him, adversity invigorates him,” Nicolas Sarkozy, head of the ruling centre-right UMP party, once wrote. Days after Mr de Villepin's appointment, 68% of respondents told Ifop, a pollster, that they did not expect him to restore confidence.

Two months on, Mr de Villepin has, by and large, steered clear of his caricature. He has made employment his priority, dropping in on a job-centre for his first official visit. He is creating a new two-year job contract for companies with fewer than 20 employees, with much-needed easy-dismissal rules, which will come into effect as soon as September. He has promised to tighten controls on welfare benefits. And he has accelerated privatisation, selling a first stake in Gaz de France in July, and announcing a controversial plan to sell three motorway-toll companies this summer.

With his visit to London this week to meet Britain's Tony Blair, Mr de Villepin has also begun to reappropriate France's counter-terrorism policy from his ambitious interior minister, who is none other than Mr Sarkozy. When he himself was interior minister, Mr de Villepin began the policy of expelling foreign imams suspected of preaching violence, and launched plans to train the rest in French language and history. His proposal to Mr Blair that European countries should share intelligence on *jihadis* who

have attended training camps in Afghanistan and elsewhere was one he had long advocated.

The electorate seems to approve. Mr de Villepin's popularity rating jumped by 11 points in July, according to Ipsos, another pollster, to 44%—well ahead of Mr Chirac's lowly 32%. The gap between Mr de Villepin and the persistently popular Mr Sarkozy has narrowed: 12 percentage points separated the two in May, according to Ifop, but the margin was down to a point in July. An arresting poll in *Paris-Match* magazine in June suggested that, in a run-off between two presidential alternatives, Mr de Villepin would beat either of the top two Socialist pretenders—François Hollande and Laurent Fabius—by only a little less than would Mr Sarkozy.

Might Mr de Villepin be shaping up as a credible successor to Mr Chirac on the right? Nothing could be less certain. The prime minister may be proving more pragmatic and focused than expected, but many an obstacle lies in the way. The public finances are under severe strain: the government is highly unlikely to keep its budget deficit below 3% of GDP next year, let alone to revive its postponed income-tax cuts. Unemployment remains over 10%. Growth remains sluggish, and consumer spending weakened in the second quarter. France still feels morose. And Mr de Villepin has yet to be tested by big street protests, which the unions are promising for the autumn.

Mr de Villepin, who worked for seven years as Mr Chirac's chief of staff, shares his faith in the faltering French social model. Mr Sarkozy may be happy to mock a model that produces mass unemployment, but Mr de Villepin believes that tinkering is enough. Thus he is ready to inject limited flexibility into the labour market, but he is not pushing for a more wide-reaching overhaul. He was the first to jump to the defence of Danone, a French food group, when rumours started of a takeover by the American giant, PepsiCo. This week he again insisted on the need for “economic patriotism”. Given the popular disillusion with Mr Chirac, the prime minister may find he is too closely tied to him to represent a credible sense of change.

But the biggest obstacle remains Mr Sarkozy. Such is the UMP boss's popularity, combined with his powers of self-belief and his talent for self-promotion, that it is sometimes assumed that nothing stands between him and the presidency in 2007. Certainly, UMP deputies, fearful for their own jobs, have gravitated herd-like to support the boss of a party originally designed solely to elect Mr Chirac—and they remain distrustful of the never-elected prime minister. Mr Sarkozy's constant taunting of the president, unthinkable were Mr Chirac not so weak, seems only to cement his popularity among voters fed up after ten years of rule by *la chiraquie*. He recently likened the president to Louis XVI, telling reporters that “I don't intend quietly to change the locks at Versailles while France revolts.”

All the same, it is another two years until the next presidential election. “One cannot assume that Sarkozy will be the only candidate on the right,” says Dominique Reynié, a political scientist at Sciences-Po. The more Mr Sarkozy adopts a populist tone and agitated manner, the more Mr de Villepin is likely to cultivate a quietly authoritative style. Even the prime minister's *hauteur* might not be a handicap. As Mr Reynié says, “the French think they embody democracy, but they have a secret fascination for monarchy: de Villepin represents a character that enjoys more approval than the French like to admit.”

History teaches that, with fratricidal division, much can change in a short time. In 1995, the right fielded two rival candidates from within the same party. One—Edouard Balladur, supported by an upcoming politician named Mr Sarkozy—enjoyed far stronger poll ratings and parliamentary support until the month before the vote. But it was the other who went on to win. His name? Jacques Chirac.

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Tour de France

Lance the conqueror

Jul 28th 2005 | PARIS
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An American in a yellow jersey

AP

A Texan in Paris

TRIUMPHANT Texans tend to go down badly in France. The victory of Lance Armstrong in this year's Tour de France, his seventh, provoked a mix of envy and admiration. The “Star Spangled Banner” ringing out on the Champs Elysées may have been hard for some, but French passion for the world's toughest cycling race, watched by 2 billion television viewers worldwide, ensures that any winner is respected. In some ways the love-hate relationship with Mr Armstrong encapsulates French ambivalence over their oldest ally.

Sure enough, *Le Parisien* wrote of his “arrogant superiority” and “cold domination”. *Le Monde* confined the story to page 17. Dinner-party talk was of old rumours (never proven) about doping, linked to Mr Armstrong's successful battle against cancer. There was much hand-wringing that no Frenchman got into the top ten—and none has won for 20 years. Yet there were also warm congratulations. “Lance for eternity” was *Le Parisien*'s headline.

These are strange times for French anti-Americanism. Politicians kicked up a stink over rumours that PepsiCo, an American food giant, might take over Danone, a French one. Yet there was barely a murmur when an American firm bought Taittinger, a French luxury group that includes the champagne and Paris's Hotel Crillon. And ordinary folk busily lap up what the elite disdains. Four of the top five box-office hits in France this year have been American. As if McDonald's cannot satisfy French fast-food appetites, KFC (once part of PepsiCo) is now spreading across France too.

The French will embrace Americans who return the favour. Benjamin Franklin and Thomas Jefferson were fêted in Paris. France made Josephine Baker a star. Mr Armstrong raced mainly in the Tour de France, saying “I have a special place in my heart for this race.” It may not be Americans who irk the French, but those who disparage Gallic virtues.

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The German election

Schröder agonistes

Jul 28th 2005 | BERLIN
From The Economist print edition

The chancellor may have his election, but not with the result he wanted

ELECTION fever is gripping Germany, even though Chancellor Gerhard Schröder's plan for an early poll on September 18th could yet fail. One hurdle was cleared on July 21st when Horst Köhler, the federal president, decided to support Mr Schröder's request, after he had engineered a lost confidence vote, to dissolve the Bundestag, or lower house. But two Bundestag members have filed suit with the Constitutional Court, which will now deliberate on whether to stop the election.

Early elections can be held in Germany only if a chancellor shows that lack of steady support in the Bundestag stops him governing. After 20 days of agonising, Mr Köhler concluded that Mr Schröder had done that. But the president's arguments left constitutional lawyers scratching their heads. “Our future and that of our children is at stake,” Mr Köhler said in his televised statement. He spoke of millions of unemployed, critical national and regional budget deficits and an outmoded federal structure. “We're having too few children and we're getting older,” he added.

These arguments are somewhat too wide, says Ernst Gottfried Mahrenholz, a law professor in Karlsruhe. He thinks the president should have stuck to the narrow question of whether Mr Schröder's claim that he could no longer govern was “plausible”. That was the issue in 1983, the last occasion when parliament was dissolved early. Then a panel of eight judges, one of whom was Mr Mahrenholz, grudgingly supported an opportunistic election called by Chancellor Helmut Kohl, but implied that things would have to be done more convincingly next time. They have not been, say Jelena Hoffman and Werner Schulz, two Bundestag members.

Udo di Fabio, a judge at the Constitutional Court, will now examine their objections. In about 14 days' time, there will be oral hearings. The court will then deliberate for a couple of weeks before making its decision, probably at the end of August, predicts Mr Mahrenholz, who recalls that the 1983 proceedings took four-and-a-half weeks in all. Yet few pundits expect the court to force a postponement of the election. Indeed, some hope that it will instead recommend a change in the constitution so that the Bundestag can dissolve itself in future without such a fuss.

Out on the hustings, Mr Schröder does not appear to have got quite the campaign he hoped for. The opposition Christian Democrats (CDU) mobilised more quickly than he had expected behind Angela Merkel, their candidate for chancellor. A new Left Party, uniting the PDS, successor to the East German communists, and WASG, a movement of discontented trade unionists, is doing well in the polls. Spice is added by the presence at its head of two political showmen: Gregor Gysi, the former PDS leader, and Oskar Lafontaine, a one-time SPD chairman and (briefly) Mr Schröder's first finance minister. The latest opinion polls give the Left Party 12% nationwide, and an impressive 32% in the east, where it could conceivably come first. These figures suggest that it is stealing votes from the SPD in the west and the CDU in the east—somewhat galling for the CDU, since Ms Merkel comes from the east.

Calculations about who might form a coalition with whom have become muddy (see article). Even the liberal Free Democrats (FDP), masters of many previous coalitions of right and left, could end up on the shelf. That would be a pity, since their programme has the boldest proposals for tackling Germany's structural and economic problems: cutting corporate tax, simplifying income tax, easing labour and environmental laws, and charging fees for higher education. Cynics say that the FDP can afford to propose such tough policies only because it will not be called upon to implement them.

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Coalition-building in Germany

All together now

Jul 28th 2005
From The Economist print edition

The beguiling talk of a grand coalition

IF THE Left Party does as well in the German election as the polls suggest, it will hugely complicate coalition-building. Its base may be the disaffected left, but it could deprive the centre-right Christian Democrats (CDU) and Free Democrats (FDP) of a majority. Hence talk of a "grand coalition", defined as one of the CDU and the Social Democrats (SPD). The seductive idea that sensible politicians from both sides should come together for the greater good is a hardy perennial in Germany. Experience suggests it would be no panacea.

Grand coalitions since 1960

Federal government	1966-69
State governments:	
Baden-Württemberg	1968-72, 1992-96
Berlin	1954-63, 1990-2001
Brandenburg	1999-
Bremen	1995-
Lower Saxony	1967-70
Mecklenburg-West Pomerania	1994-98
Saxony	2004-
Schleswig-Holstein	2005-
Thuringia	1994-99

Sources: Forschungsgruppe Wahlen; Federal Returning Officer

Grand coalitions have been quite common at state level ever since the birth of the federal republic. After the fall of the Berlin Wall in 1989, Berlin was governed jointly by the two main parties for a decade. Many other states have tried grand coalitions, with varying degrees of success. Today there are four (see table). But at federal level Germany has had just one grand coalition: in 1966-69, with the CDU leader, Kurt Georg Kiesinger, as chancellor, and the SPD leader, Willy Brandt, as foreign minister.

It was not a happy period. Emergency legislation failed to quell student protests. Disgruntled voters drifted towards extremists or outside politics. It was no coincidence that the Red Army Faction, a brutal terrorist group, sprang up. A more benign product was the environmentalists who later formed the Green Party. The far right also exploited the situation, with the neo-Nazi NPD securing its best-ever result in 1969, close to the 5% threshold for seats in parliament.

A second grand coalition might not provoke terrorism, but it could bring problems of its own. It would tend to soggy compromise on much-needed economic reforms, the more so since a disgruntled SPD would be junior partner. Time in opposition might rejuvenate the Greens. The Left Party would like nothing better than to take potshots at a grand coalition from the wings, raising its hopes of becoming a third political force. The NPD might be helped across the 5% threshold.

All this would depend on somebody, presumably the CDU's Angela Merkel, actually being able to form a grand coalition. But a battered SPD under a new leader, perhaps its chairman, Franz Müntefering, would surely feel resentful of the CDU, not least for having blocked much of the present SPD-led government's plans in the upper house, or Bundesrat. If the SPD prefers opposition, creating any workable government may be hard. In theory a CDU-FDP-Green coalition is possible, but the culture clash between the parties makes it unlikely. Nobody wants to ally with the Left Party. A grand coalition may be unattractive, but if voters deny the CDU-FDP a majority, it may be unavoidable.

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Croatia's Serbs

Stormy memories

Jul 28th 2005
From The Economist print edition

Marking the tenth anniversary of Croatia's recapture of Krajina

IT HAS been a month of anniversaries in the former Yugoslavia. Three weeks ago world dignitaries gathered in Srebrenica to commemorate the killing of some 8,000 Bosnian Muslims by Serb forces. The next anniversary will receive much less attention. Yet Operation Storm, the Croatian military assault on Krajina, the would-be secessionist Serbian state in Croatia, with its capital at Knin, has left deep scars.

The attack, which began on August 4th 1995, triggered the flight of as many as 200,000 Croatian Serbs. Within hours vast convoys of Serb refugees were choking the roads of northern Bosnia. Franjo Tudjman, Croatia's then president, exulted that Croatia's Serbs had “disappeared ignominiously, as if they had never populated this land. We urged them to stay, but they did not listen to us. Well then, bon voyage!”

Before the war some 600,000 Serbs lived in Croatia, making up 12% of the total population. According to the census of 2001, only just over 200,000, or 4.5% of the population, live there today. Reliable and up-to-date figures are hard to find. The Organisation for Security and Co-operation in Europe reckons the number may be higher, pointing out that many Serbs do not want to identify themselves as such. The Croatian government claims that some 95,000 Serbs have returned from other countries in the past ten years. But as many as 40% have come back on paper only. They have reclaimed their Croatian citizenship and their property—and promptly left again.

Sasa Milosevic, the programme director of the Serbian Democratic Forum in Zagreb, which helps returnees, believes that the 2001 census figures are broadly right, and that Serb numbers are now falling because so many who did return were old. He thinks another 150,000 Serb refugees are still in either Serbia or Bosnia. But one survey found that only 14% of those who had not yet gone home might still do so one day. The rest have become citizens of Serbia, Bosnia or whichever other country they fetched up in.

It all sounds gloomy; yet there are hopeful signs. The prime minister, Ivo Sanader, has worked hard to reach out to remaining Croatian Serbs, not least because his government relies on the votes of Serb deputies. Much has been done to return property to those who fled, to the extent of evicting Bosnian Croats who settled in Serbs' houses. This, says Andrea Feldman, director of Croatia's Open Society Institute, represents “the turning of a new page”. This week, too, Montenegro became the first ex-Yugoslav entity to agree to pay war compensation, offering Croatia €385,000 ($460,000) for cattle

taken by its soldiers in June 1991.

The biggest problems for Croatian Serbs are the weak economy and job discrimination. Some hesitate to return from Serbia, whose economy is in even worse shape, because they fear arrest as indicted war criminals. But this issue is now being cleared up. Bosnia, Serbia and Montenegro, and Croatia have agreed to try to close remaining refugee issues by the end of 2006. One thing they want to do is to reduce the number of refugees who register to return home, reclaim property and collect pensions, but still maintain their registration as refugees, so as to collect what meagre social help this status gives them.

This year a sense of bitterness will pervade Croatia's anniversary celebrations. As Croatians see it, Operation Storm liberated Serb-held land. But now Croatia cannot begin European Union entry negotiations because Ante Gotovina, the general who led Operation Storm, is wanted by the war-crimes tribunal in The Hague on charges of murder and ethnic cleansing. Since Croatia has not arrested him, talks with the EU remain frozen.

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Spain and Islam

Al-Andalus revisited

Jul 28th 2005 | GRANADA
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Fear of Islamist terror casts shadows on the country that expelled the Moors

AFP

Back in Granada, 510 years on

ALL of Europe, it seems, is fretting about its Muslim population. Spain's is relatively small—less than a million—yet no country has a more complex relationship with Islam. Until two years ago, the muezzin's cry "Allahu akbar" had not been heard in Granada since the *reconquista* and the expulsion of the last Moorish king in 1492. But then a mosque was erected in the Albaicin quarter near the Alhambra. For the mainly Spanish converts to Islam who built it, this was the dawn of a new era: as a mosque spokesman put it, "the seeds of Islam were planted long ago, and now they are flourishing once again."

Although some traditionalists resisted the mosque, it is not the "heritage" strain of Islam that really preys on Spanish minds: it is the new, fundamentalist variety. This was brought home most shockingly after Islamist terrorists bombed the trains in Madrid in March 2004. Now the London bombings have revived fears. Shortly after the Madrid attacks it seemed that Spain might follow France's example by waging war on radical Islam. The interior minister, José Antonio Alonso, announced plans for more police in cities with large Muslim populations, to crack down on mosque-building and *jihad*-preaching imams. But in keeping with the conciliatory nature of the new Socialist government of José Luis Rodríguez Zapatero, these plans have been shelved.

Instead, a board has been set up for the Foundation of Pluralism and Peaceful Coexistence, based on accords signed between the government and Islamic, Jewish and Protestant representatives in 1992. Mercedes Rico Carabias, director-general of religious affairs and member of the board, insists that Spain has moved away from the restrictive French model of allowing only state-approved mosques. "It is very important that the Muslim community is not put under suspicion," she says. Instead, she hopes to give Islam the same status as other religions. "In Spain, the problem is plurality. We have now changed from being a totally Catholic country, and we have to respect that."

The chief task of the foundation is to bring Islam into mainstream society by such means as paying for social programmes and encouraging imams to learn Spanish. Groups such as the Moroccan Immigrant Workers' Association had complained that financing of mosques was in the hands of Saudi-backed imams who preached radical Islam. The government wants public financing of mosques, but this is against the law. Ms Rico says that "we must find another way, either with private or international money, to finance mosques in the future." Even secular academics, such as Joan-Francesc Pont Clemente, at Barcelona University, agree. "An absolute separation between church and state would not be useful," he says. "Above all, since Islam has appeared as an important religion. We cannot close our eyes to Islam and end up letting it be financed entirely by Saudi Arabia or radicals."

Spain's relationship with Muslims remains loaded with historical baggage. The vision of the country as a bulwark against barbarism, the expulsion of the Moors and the persecution of Muslim Spanish converts by the Inquisition are all cherished by both the right and the Catholic church. Their views were bolstered by the call from al-Qaeda, both before and after the Madrid bombs, for a holy war to "liberate al-Andalus". José María Aznar, the centre-right prime minister whose party was swept from power after the bombings, also calls on history. "There are those who think that the Madrid attacks are related to the support given by the Spanish government to the Iraq war," he said in a speech in Washington, DC, last year. "The problem with al-Qaeda came from before that—as long ago as 1,300 years."

Attitudes on both sides remain ambivalent, however. Surveys have repeatedly shown that North Africans top the charts of people that Spaniards most distrust. Last year there were violent protests in at least three towns against the opening of “garage-mosques”. Yet another recent survey, in *El País*, put Moroccan men first as Spanish women's preferred choice of marital partners among foreigners. The admirable al-Andalus notion of *convivencia*, or peaceful coexistence, is once again challenging Spain.

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Charlemagne

Of head and heart

Jul 28th 2005
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Charlemagne retires, in some confusion

REGULAR readers may notice a new clarity and vigour in the thinking of the Charlemagne column when it returns in September. The present author is returning to London, after almost five years in Brussels, and a fresh pair of eyes is arriving from Washington, DC.

It is a good time both to be leaving and to be arriving. This summer has been marked by perhaps the most dramatic rebuff to the European project since its foundation: the rejection by French and Dutch voters of the first-ever unified, written constitution for the European Union. The French and Dutch referendums seem to mark the end of a great wave of European unification that set off with the construction of a proper single market in the 1980s, and continued through the creation of a single currency and a common foreign policy in the 1990s. A new and unpredictable period is opening—hence the past few weeks' exaggerated talk of the EU being in deep crisis.

Your correspondent arrived in Brussels as something of a Eurosceptic. The essential argument of the sceptics is that it is a mistake to try to create a political union in Europe, on the basis of very shallow popular consent. Most Europeans feel much more ultimate loyalty to their nation-state than they do to Europe. Opinion polls tell you this; so does simple observation of daily life. Europeans speak many different languages, watch different television programmes, respond to different politicians and draw meaning from different traditions and memories. Of course, they also share many common interests and values, which can form the basis for fruitful co-operation, not least within the EU. But push political integration too far, and you will spark a backlash. That is what a Eurosceptic would have predicted in 2001. And that is what seems to have happened with the French and Dutch votes.

Lest this sound intolerably smug, however, your correspondent should admit that he leaves Brussels feeling more confused than when he arrived. That is because dry analysis is never quite enough when dealing with the EU. Most people who feel strongly about the subject start with a gut feeling—from which flow their subsequent arguments about such topics as the merits of a European single currency or the need for harmonised court procedures. Charlemagne's problem is that over the course of nearly five years in Brussels, head and heart have begun to diverge. The head still says that it is wrong to pursue deeper political integration in Europe; the heart is more sympathetic to the idea, or at least to its advocates. The head greeted the French rejection of the constitution with a feeling of relief that a bad proposal had been shot down; but the heart sank at pictures of the far-right National Front celebrating wildly, while educated, liberal internationalists were struck dumb with shock.

Why this sliver of sympathy for the European ideal? Partly, it is a matter of exposure to non-British views of the future of Europe. For the British, Europe has always been a matter of the head, rather than the heart. They joined the then EEC for essentially economic reasons, and have traditionally regarded the aspiration for political union in Europe as silly, if not downright sinister. In 1990, when Nicholas Ridley, a cabinet minister in the Thatcher government, was forced to resign after likening the contemporary German aspiration for political union in Europe to the ambitions of the Nazis, he was probably speaking for more Britons than liberal opinion cared to acknowledge.

After living in Brussels, however, it can be confirmed that most advocates of political union are not, in fact, neo-Nazis. On the contrary, European federalists tend to be highly idealistic. They are usually driven by the belief that political union is the best way of ensuring lasting peace and prosperity on the continent. Given Europe's blood-soaked history, that is a noble aspiration. And while peace in western Europe can now probably be taken for granted, the enlargement of the EU to take in countries from the former Soviet block—and, perhaps, to admit the Balkans and Turkey over the next decade—has given a new validity to the EU's original mission. The ambition to “join Europe” has been crucial in helping to cement stability and prosperity in the post-Soviet states of central and eastern Europe. For somebody used to the jaded anti-Europeanism of modern Britain, it was both impressive and educational to

witness the appeal of Brussels to the new democracies in the region.

Dreams and reality

Support for enlargement of the EU does not, of course, necessarily mean support for political union. Indeed, many Britons like enlargement precisely because it has made a political union less likely. All the same, the success of enlargement is an important corrective to two of the emotions that often underpin Euroscepticism: a quiet rejoicing in any setback for the EU, and an impatience with the idea that the notion of "Europe" can exercise a positive, emotional pull.

Of course the European ideal also has less attractive aspects, such as the streak of anti-Americanism that often lurks beneath the surface. Brussels officials also easily confuse their own interests with those of humanity at large. But even Eurocrats can be unfairly abused. Doubtless there is scheming and corruption in Brussels. But your average Eurocrat is mild-mannered, well-educated, multilingual and committed to the idea of international co-operation. If all Europeans were as cosmopolitan as the average EU civil servant, building a political union in Europe would be a doddle. The trouble is that the Eurocrats are creating a political system that makes perfect sense to them—but seems impossibly remote to the average stay-at-home German, Pole or Briton. That is why the rejection of the constitution by French and Dutch voters feels like the end of the dream of political union. It was, in some ways, a beautiful dream. But, in the end, it is better to live in the real world.

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America's labour federation

Losing its grip

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From The Economist print edition

Getty Images

Will the split in the AFL-CIO hurt organised labour, or reinvigorate it?

JUDGED by oratory alone, this week's convention of America's labour federation, the AFL-CIO, in Chicago was a triumph. Teddy Kennedy railed against the "most anti-worker, anti-labour, anti-union administration in memory". Barack Obama, the Democrats' new black hope, dreamed of when "labour rises again". Nancy Pelosi blasted free trade. John Edwards scolded chief executives for their "golden parachutes". The Rev Jesse Jackson called for "massive ground action". Everybody booed Wal-Mart.

Alas for labour, such firebreathing paled in the face of the AFL-CIO's own troubles. On July 25th, two of the three biggest unions withdrew from the labour federation. The Service Employees International Union (SEIU) and the Teamsters, who cover freight-shippers and associated trades, think they have a better way to rebuild the union movement, which has seen membership fall to 12.5% of the total workforce in 2004 from over 30% in the 1950s (see chart below). Last year, just 8% of private-sector workers were unionised. The dissident "Change to Win" coalition now comprises seven unions. Two of them, UFCW (food and commercial workers) and UNITE HERE (clothing, hotel and restaurant workers) also boycotted the convention and could defect from the federation soon.

For the AFL-CIO, this is a bad blow. The federation was just marking its 50th anniversary at this week's convention. The irony was painfully apparent. In 1955, in New York, the American Federation of Labour and the Congress of Industrial Organisations merged after years of bickering; today that alliance has split apart, at a time when Social Security, an increased minimum wage and other things dear to the unions are under assault from Republicans in Washington. Union leaders report harassment, threats and even firings when they exercise their rights to organise. Convention delegates this week voiced support for John Sweeney, who has been president of the AFL-CIO for 10 years. He was due to be re-elected in an uncontested election on July 27th. But the breakaway unions say that Mr Sweeney's record, as essentially a steward of decline, leaves no hope.

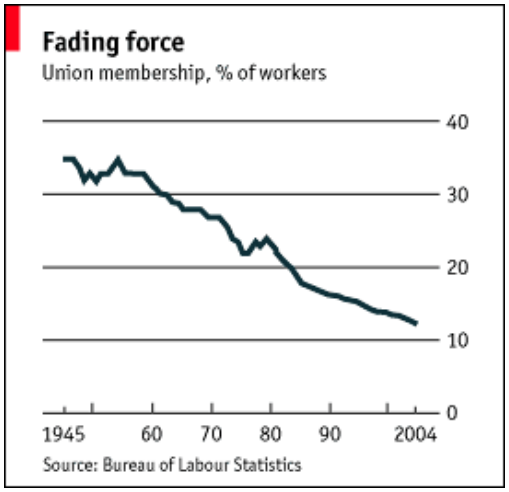
Do the rebels stand a chance of reinvigorating the union movement? "The most important thing to remember is that American unions are pretty autonomous," says David Levine, a professor at the Haas School of Business at the University of California at Berkeley. "The AFL-CIO shows up publicly in newspapers, but it actually doesn't do very much to affect members' lives." Indeed, the federation spends about one-third of its money on political activities.

Virtually alone among the unions, the SEIU has seen its membership soar, from 625,000 in 1980 to

1.8m today (including about 50,000 in Canada). The Teamsters' membership has stayed steady, around 1.4m, since the current president, James Hoffa junior, took office in 1999. By contrast, numbers in the United Steelworkers of America plunged by 100,000 between 1998 and the beginning of 2005, despite strong organising drives.

What is the SEIU's secret? Luck, partly: the service sector is a fast-growing part of the economy, and it is hard to outsource the jobs of caretakers and bus drivers. But Andrew Stern, the head of the service employees and leader of the dissidents, also claims new tactics. In 2001 he managed to unionise many of New Jersey's caretakers by persuading their firms that the union demands would take effect only if 55% of firms agreed (ie, they would not be undercut by competitors). His other ideas include organising by industry—so that, say, doormen and croupiers could join forces in the gaming industry—and more accountability for organisers. Most ambitiously, Mr Stern wants to create global union links, so that workers in Europe could agitate on behalf of their American counterparts, and vice-versa.

Some personal bitterness lies behind the break-up. Mr Stern worked as the organising director for Mr Sweeney until the mid-1990s, when Mr Sweeney headed the SEIU. His former boss called the boycott of the convention an “insult”. Yet the insurgency is already spurring change at the AFL-CIO. Mr Sweeney and his henchmen are suddenly talking about more “accountability” and organising by industry, and aim to double the budget for membership drives to $22.5m. Campaigns are coming against Wal-Mart, Comcast, Clear Channel and Toyota. But all this seems not enough for Mr Stern, and it may bump into cold reality in any case, since the federation will have $18m less in annual membership dues after the defections.



What does the split mean for American politics? In terms of which candidates the unions will support, probably very little. Though Mr Stern vows that his members will not be “lapdogs for any political parties”, he is also unlikely to start backing Republicans willy-nilly. He is scathing when it comes to CAFTA, the Central American Free Trade Agreement, which at last squeaked through the House of Representatives this week. “We were sold the biggest fraud in history, that trade would be good for American workers,” he says of America's trade policy.

Even so, the split is “not good news” for Democrats, says Robert Reich, who served as secretary of labour under Bill Clinton. Traditionally, he says, unions have served as the party's ground troops, just as the religious right now does for the Republicans. About a quarter of voting households belong to unions. Their backing, though circumscribed by the McCain-Feingold campaign-finance reforms, gives Democrats a big boost in national races—the AFL-CIO poured $44m into John Kerry's presidential campaign last year, and unions can also sometimes have a big impact locally, as in the New York and Los Angeles mayors' races. With a split, says Mr Reich, Democrats will have to deal with competing groups of labour executives with potentially different priorities. Also, if Change to Win carries out its promise to spend more on organising, that will mean less money for politicians.

Longer-term, though, all may not be lost for the Democrats. If Andy Stern and other dissenters have a formula for dramatically increasing union membership, that could help the party, says Mr Reich. Rivalry among the two factions could also end up boosting membership (so long as they do not raid one another's unions). Mr Levine of Berkeley points out that the union movement “started declining at almost exactly the moment that the AFL and the CIO unified”. One small part of the cause, he suggests, might be that when they were separate organisations, they competed against each other. Will history

repeat itself, in reverse?

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The San Diego mayor's race

A dubious prize

Jul 28th 2005 | SAN DIEGO
From The Economist print edition

Under the shiny surface, a real mess awaits the victor

PITY the next mayor of San Diego, which once proclaimed itself “America's finest city”. With a pension deficit of at least $1.4 billion, the seventh-largest city in the country is now on the edge of bankruptcy; its financial affairs are the subject of investigation both by the Justice Department and the Securities and Exchange Commission; the city can raise no new money because independent auditors are refusing to certify the books; and two city councilmen, convicted last week of corrupt dealing with a strip-club owner, face jail. No wonder Dick Murphy, controversially re-elected mayor in November, announced in April that he would leave office on July 15th, more than three years early.

The question is whether Mr Murphy, a mild-mannered former judge, will be succeeded by Donna Frye, a 53-year-old councilwoman who entered politics as an environmental crusader, or Jerry Sanders, an amiable 54-year-old who for six years was the city's police chief. In an 11-candidate primary on July 26th, Mrs Frye, dubbed the “Surfer Chick” because she owns a surf shop with her husband, won a handsome 43% of the votes. Mr Sanders won 27%, beating off the well-financed challenge of businessman Steve Francis, who had hired experts from Governor Arnold Schwarzenegger's campaigns and had taken to the TV screens with negative advertising.

In theory, then, Mrs Frye is the favourite for the run-off scheduled for November 8th. Indeed, many would argue she should already be in office. In last November's election she was a “write-in” candidate and, after much litigation, lost to Mr Murphy by a mere 2,108 votes—but only because 5,551 of the 155,000-odd who wrote her name on the ballot paper had neglected to mark the oval box next to it.

Yet the pundits are not so ready to dismiss Mr Sanders. Come November, they argue, Mrs Frye may appear too liberal a Democrat to appeal to the majority of San Diego's voters. By contrast, Mr Sanders will get the Republican vote, including the 23% who this week opted for Mr Francis, and perhaps the votes of some Democrats, too. After all, his reputation as an effective police chief—he claims a 40% drop in crime during his tenure in the 1990s—lives on.

Both candidates recognise there is no easy solution to problems that began when the council in 1996 and 2002 voted to increase pension benefits but not pension contributions. To her credit, in 2002 Mrs Frye was the lone voice on the nine-member council opposing the increase in benefits. As mayor, she would ask the courts to appoint an independent receiver to re-organise the pension plan; she would cut subsidies for downtown development; and she would pursue a policy of open government, with public meetings of the council at least twice a month. For his part, Mr Sanders would cut jobs in the city bureaucracy and would negotiate new pension deals with the public employees' unions, including raising the retirement age and the level of employee contributions. Neither candidate likes to mention one obvious remedy: raising taxes.

In the meantime, San Diego—so sunny and prosperous on the surface—carries on, with families strolling through Balboa Park and weekend sailors scudding across Mission Bay. The optimists point to a buoyant property market and the region's cluster of high-tech investments. Who cares if the city council, now down to six after the departure of Mr Murphy and last week's conviction of two of its members, risks unbreakable deadlock (five votes are needed to make a decision)?

Yet at some point the financial failings will intrude on the public consciousness. Pessimists note a decline in public services, including police and fire departments that are now among the nation's smallest per number of residents. In October 2003, when a wildfire raged through San Diego County, the city had no helicopters to fight it; this year there was not enough money to repair all the potholes after the winter rains. Mrs Frye, proud of her long experience as a councilwoman, has perhaps the most comforting slogan for this glossy but battered city: “No training wheels required”.

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South Carolina

Laying ghosts

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Hate, reconciliation and secession

FOR YEARS, South Carolina has floated near the bottom of national rankings for education, income, growth and so on. It has got rather used to it by now. But in one thing the Palmetto State excels: it has more hate groups than anywhere else. A recent report by the Southern Poverty Law Centre (SPLC), a watchdog body that battles discrimination through the courts, says South Carolina boasted 47 hate groups last year, more than Florida (43), California (42) Georgia (41) or Texas (40).

Across the country, the Centre's Intelligence Project counted 762 hate groups and 468 hate websites in 2004. (The number of groups has gone up slightly, from 751 the year before; the number of websites has fallen, from 497.) The latest number for groups continues an upward trend: in 1997, Centre staff identified only 474 active ones. They include black separatists, Ku Klux Klanners, neo-Nazis, racist skinheads, Christian identity members, neo-Confederates and, ominously, “Other”.

South Carolina's high ranking stems partly from its many League of the South (LOS) chapters. The LOS, a neo-Confederate organisation founded in 1994, seems to attract academics. J. Michael Hill, a former professor and a founder of the group, is a specialist in Celtic history. He stoutly denies that his group is a hate group, or racist either.

But the LOS had a big hand in trying to keep the Confederate flag—a blatantly racist symbol to most blacks—flying over the South Carolina statehouse. (It was finally taken down a few years ago, after decades of controversy.) And the group, which advocates seceding from the United States just as its members' forebears did in 1860, is proud of its role in helping to eject Governor David Beasley from his job, in 1998, because he wanted to take the flag down.

The SPLC's disheartening report comes at a time of better news in race relations, both nationally and in South Carolina. Last month, the United States Senate formally apologised for failing to pass legislation that would have made lynching a federal crime. Nearly 5,000 people, mostly black men in the racially segregated South, are known to have been lynched between the 1880s and the 1960s.

Meanwhile, in Abbeville, South Carolina, a startling church service was held earlier this month during which a number of whites confessed openly that their ancestors had carried out lynchings and kept slaves. Abbeville, a town in the north-western part of the state, is known as “the cradle and grave of the Confederacy”; it witnessed both the first meeting of secession, in 1860, and the last cabinet meeting of Jefferson Davis, then-president of the dying Confederacy, in 1865.

In October 1916, hundreds of white Abbeville citizens set upon Anthony Crawford, a prosperous black farmer who had dared talk back to a white man. After beating Crawford, the crowd strung him up to a pine tree. Then, for good measure, a firing squad of about 60 whites riddled his swinging corpse with bullets.

Some of Crawford's descendants attended the service in Abbeville. They said they had forgiven the white mob for its crimes. But the ghosts of the region's past have not yet been laid. Abbeville played host to the national conference of the LOS in both 2002 and 2003. Mr Hill, one of its founders, has called slavery “a God-ordained institution”.

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New York politics

Goodbye, George

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The governor clears the way for Eliot Spitzer

QUACK, said George Pataki this week, declaring himself a lame-duck governor of New York. After three terms in office he would not seek a fourth next year, he said.

That more or less promises the job to the Democratic challenger, Eliot Spitzer, New York's swashbuckling attorney-general, who has been leading Mr Pataki, a Republican, handsomely in the polls. The Republicans, a minority in the state, have no other obvious candidate with even a ghost of a chance—a measure, critics would say, of Mr Pataki's neglect of the party.

His admirers, such as they are, hope still that he plans to run for the presidency in 2008. He was silent on that this week, though ten days earlier he went noisily to Iowa, a vital early state, seemingly to test the air. It is hard to see him getting very far. With his support for gun control and for some abortion choice he is, as one analyst put it, “a blue-state Republican in a red-state party”. The *National Review*, a conservative weekly, has said he “walks softly but doesn't even carry a toothpick.”

Even if the Republican Party does come to decide that it wants a moderate presidential candidate in 2008, it will have another New Yorker to hand in the shape of Rudolph Giuliani, Michael Bloomberg's predecessor as mayor. The terrorist attacks of September 11th 2001 made Mr Giuliani a national hero. For Mr Pataki, they have meant years of public impatience with the rows and redesigns dogging redevelopment of the World Trade Centre site, which falls partly under New York state jurisdiction.

Mr Pataki is doing the right thing by going gracefully. If he ran and lost to Mr Spitzer next year he would have an even slimmer chance in 2008. But barring a last-minute miracle, his legacy will be nothing to brag about.

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The UN Security Council

United we stand

Jul 28th 2005
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An unexpected agreement on expansion

THE Americans may have miscalculated. Their attempt to nip reform of the United Nations Security Council in the bud has been foiled—for the moment at least. This week, the momentum for a bigger, more representative council got a vital new fillip when the four countries pressing for permanent seats—Japan, India, Brazil and Germany—clinched an agreement with the 53-member African Union (AU) to present a joint resolution on expansion to the General Assembly, thereby greatly increasing its chances of success.

Hitherto, the Africans had been insisting on seven new council seats for Africa, including two permanent ones with full veto powers. But at a last-ditch meeting in London on July 25th, the foreign ministers of the so-called Group of Four (G4) managed to persuade their AU counterparts that holding out for veto rights would scupper all chance of reform. They themselves have already agreed to abandon their pretensions to such rights.

As a quid pro quo, the G4 has agreed to accept the AU's proposal for an extra 11 new members, instead of the ten it was proposing, bringing total Security Council membership to 26. Besides the six new permanent members, on which both groups are agreed—two from Africa, two from Asia, one from Latin America and one from Europe—there would be five new non-permanent members elected for two-year terms—one each from Africa, Asia, Latin America and eastern Europe, with a fifth assigned to the developing countries.

The AU is expected to call for a summit in Addis Ababa next week, at which it hopes to get the necessary two-thirds approval of its own members for the new position. A joint resolution has already been drawn up, which the G4 and AU hope to put to the General Assembly before the UN summit on September 14th-16th. But timing is tight. Many delegations to the UN close shop during August. Their absence would make it even more difficult to win the two-thirds vote of the UN's 191 members required for any charter amendment. So the two groups may decide to defer a vote until early in September.

They claim to be confident of success. But the closer they get to achieving their goal, the greater the opposition will be. Many of their most ferocious opponents, including Pakistan, Italy, Spain, Colombia, and Mexico—though not China—have joined together, in what is unofficially known as the “Coffee Club”, to put forward a rival proposal involving the addition of ten new members to the council, all non-permanent. But it has little support outside their own ranks.

For a long time, America, which would probably prefer to maintain the status quo, declined to join in the debate other than to say that it supported Japan for a permanent seat. Last month its under-secretary of state for political affairs, Nick Burns, appeared to open the door a little further by suggesting that America might be willing to consider “two or so” new permanent members, plus “two or three” new non-permanent ones, bringing the total membership to 19 or 20.

But in evidence last week to the Senate Foreign Relations Committee, Mr Burns lashed out at the G4's proposals, calling them “highly divisive”, saying that America would vote against them and urging others to do the same. Indeed, he suggested that any attempt at Security Council reform at this stage would not be “timely”, serving merely to distract from more urgent matters. Some fear that the United States could still block the whole process. But others are beginning to believe that, perhaps, it may not be able to.

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Evolution and schools

Intelligent design rears its head

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It's subtler than creationism, and may be coming soon to a classroom near you

SOMETIME within the next few months, the Kansas Board of Education will decide whether to allow a form of creationism to be taught in the state's schools. It seems likely to do so. The proposed curriculum changes have been given preliminary approval by the board and were written after hearings dominated by anti-evolutionists.

The changes, which affect the standards used in statewide science tests, include adding the word “may” to the assertion that “gradual changes...over many generations may have resulted in variations among populations and species.” They would tell students that “in many cases the fossil record is not consistent with gradual, unbroken sequences postulated by biological evolution.” And they would call the notion that one species evolved from another “controversial...based on inferences from indirect or circumstantial evidence.”

None of these propositions is false. But the cumulative effect, as some members of the board themselves approvingly noted, would be to encourage teachers to discuss alternatives to evolution—a theory one member, Connie Morris, has dismissed as “a fairy tale”.

Kansas is one of many states where teaching evolution is under attack. In Georgia's Cobb County, for instance, the local school district stuck labels on textbooks saying “Evolution is a theory, not a fact”. It was told to remove them by a district judge. Georgia's state superintendent of schools proposed removing the E-word altogether from the biology curriculum, though she later backed down.

In Pennsylvania, the state House of Representatives is discussing a bill to introduce an alternative to evolutionary theory into the public-school code, while Dover, Pennsylvania, has become the first district in the country to adopt the following guideline: “Students will be made aware of gaps/problems in Darwin's theory and of other theories of evolution including, but not limited to, intelligent design.” This being America, a trial is due to begin in September to decide whether that guideline contravenes the first amendment, which bans state sponsorship of religion. In all, disputes involving evolution are bubbling in around 20 of the 50 states.

It is tempting to see this as one more example of the surging influence of the religious right. But that is only partly true. The battles over evolution are being fought in secondary schools; there is no argument at universities, where evolutionary science is uncontroversial.

Nor are there signs of any recent increase in popular opposition to teaching evolution. In 1999, the Kansas guidelines were even less scientific than they could soon become; back then they omitted all reference to evolution, the age of the earth or anything inconsistent with old-fashioned creationism. They changed because creationists were removed from the Board of Education in elections in 2000. A new board rewrote the guidelines to bring them into line with accepted science, but that board was in turn removed in 2004, bringing back an anti-evolutionist majority, along with pressure to change the guidelines again.

The implication is that anti-evolution in America is a persistent rather than a resurgent phenomenon. It ebbs and flows. The reason for its increase now has less to do with any fundamentalist backlash than with the lobbying power of proponents of a theory of evolution called “intelligent design”.

Intelligent design derives from an early-19th-century explanation of the natural world given by an English clergyman, William Paley. Paley was the populariser of the famous watchmaker analogy. If you found a watch in a field, he wrote in 1802, you would infer that so fine and intricate a mechanism could not have been produced by unplanned, unguided natural forces; it could have been made only by an intelligent being. This view—that the complexity of an organism is evidence for the existence of

God—prevailed until 1859, when Charles Darwin's "Origin of Species" showed how natural selection could indeed "explain so many classes of facts" (as Darwin put it).

Proponents of intelligent design are renewing Paley's argument with a new gloss from molecular biology. Darwin himself acknowledged that "If it could be demonstrated that any complex organ existed which could not possibly have been formed by numerous, successive, slight modifications, my theory would absolutely break down." Intelligent designers claim that living things are full of such examples at the molecular level. Blood clotting is one: ten proteins have to work together in sequence for the process to occur. So-called eukaryotic cells, which digest nutrients or excrete waste, are another: these cells contain an elaborate "traffic system" which directs proteins to the right compartments.

In both cases, argues Michael Behe, whose book "Darwin's Black Box" is one of the bibles of intelligent design, you have complex systems that will work only if all the components operate at once. He argues that you could not get such a thing from "successive, slight modifications". Hence the molecular machines inside living beings are evidence of an intelligent designer—God.

Intelligent design asks interesting questions about evolution, but since all its answers are usually "God", scientists have rejected it. As the National Academy of Sciences has said, intelligent design "and other claims of supernatural intervention in the origin of life" are not science because their claims cannot be tested by experiment and propose no new hypotheses of their own. (Instead, intelligent designers poke holes in evolutionary theory.)

In addition, biologists point out that the intelligent designers' favourite examples of "irreducible complexity" often prove not to be. Some organisms, for example, use only six proteins to clot blood—irreducibility reduced. In other cases, single parts of a complex mechanism turn out to have useful functions of their own, meaning that the complex mechanism could have been produced by step-by-step evolution. When the Discovery Institute, a promoter of intelligent design, came up with a list of 370 people with science degrees who backed their ideas, the National Centre for Science Education responded with almost 600 scientists called Steve or Stephanie who rejected them.

But if intelligent design has few friends among scientists, it has won a significant following among the general public. There are a couple of reasons for this. First, evolution itself seems to stick in the craw of anyone with strong beliefs, not just those who are religious. Stalin's Soviet Union rejected evolution, for example, on the ground that only economic conditions could be said to determine human behaviour. The Nation of Islam, an American Muslim group, also rejects it.

Religious conservatives have a special reason for disliking natural selection. There may be nothing necessarily anti-Christian about Darwin's theory (which was hailed by Charles Kingsley, a contemporary clergyman, as evidence of the majesty of God), but if God has a plan for the world and everyone in it, as most American Protestants and President George Bush say they believe, then it is much easier to imagine evolution occurring under divine guidance than as a result of random mutations and the survival of the fittest. By providing an explanation consistent with those beliefs, intelligent design has proved tempting to conservative Christians everywhere, not just in America.

In early July, Christoph Schönborn, the cardinal archbishop of Vienna, rejected "the supposed acceptance—or at least acquiescence—of the Roman Catholic Church" in "neo-Darwinian dogma". He conceded that "evolution in the sense of common ancestry might be true", but argued that "evolution in the neo-Darwinian sense—an unguided, unplanned process of random variation and natural selection—is not." The Catholic Church has long turned its back on a literal reading of the Book of Genesis. It does not seem to be doing the same with intelligent design.

Second, though there has been no big increase in opposition to evolution, there is enough to be going on with without it. Two-thirds of Americans think humans were directly created by God (as opposed to 22% who think people "evolved from an earlier species"). Half do not think apes and men had a common ancestor.

With its claims (however spurious) of scientific respectability, intelligent design promises to reconcile mass anti-evolutionism with science. Strict creationism has been long discredited and, since the Supreme Court decision of *Edwards v Aguillard* (1987), may not be taught in state schools. But intelligent design is a different matter. Its proponents accept that the earth is billions of years old. They agree that gene mutation and natural selection occur within species, though not necessarily between species. They concede that scientific method, not biblical authority, is the arbiter of truth. Proponents do not even demand that intelligent design should replace evolution in the classroom, merely that schools should "teach the controversy" (which they themselves have created). In short, religious Americans who find evolution distasteful are jumping at the chance to teach an alternative that claims to be science.

Whichever way the argument over intelligent design is finally resolved, it is likely to damage science teaching. This is not because bad science standards will necessarily be adopted but because—as Diane Ravitch of the Brookings Institution showed in “The Language Police” in 2003—the biggest threat to high standards is the unwillingness of state Boards of Education to offend any sort of pressure group, whether right or left. Instead, they avoid controversial topics altogether. In 2000, a survey by the Fordham Foundation found that only ten states taught evolution fully, six did so skimpily and in 13 the treatment was considered useless or absent. (Kansas received an F minus, and “disgraceful”.) These failings shame American evolution teaching, and the manufactured controversy over intelligent design will do nothing to make them better.

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Lexington

The case of the hapless toad

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John Roberts's critics should focus on the commerce clause, not on Roe v Wade

EVER since the Supreme Court legalised abortion on demand in 1973, *Roe v Wade* has haunted Republican Supreme Court nominations. The Democrats' determination to defend *Roe* against its critics has been heightened by widespread suspicions, shared by many liberal as well as conservative legal scholars, that the decision was poorly grounded in the constitution. But this time round, *Roe* could well be eclipsed by a far more technical issue—the clause of the constitution that allows the federal government to regulate interstate commerce.

This is not because the pro-choice forces are silent. Less than an hour after George Bush introduced John Roberts—complete with radiant wife and gambolling children—Nancy Keenan, president of NARAL Pro-Choice America, was on the phone to journalists denouncing Mr Roberts as an “anti-choice nominee”, and activists are already on the march on Capitol Hill.

Nor are the pro-choice forces bereft of evidence. Newly released documents from Mr Roberts's time in the Reagan Justice Department suggest that he endorsed the legality of various Republican bills that would have stripped the Supreme Court of its jurisdiction over abortion. In 1991 the young John Roberts signed a brief on behalf of George Bush senior challenging the constitutional right to one. Both he and his wife are devout Catholics, and Mrs Roberts is also an active member of an anti-abortion group called Feminists for Life.

But Senate Democrats have good reason to distance themselves from pro-abortion activists. This is partly because the case against Mr Roberts is weak. His 1991 brief is dispassionate, and merely represents the long-standing view of Republican administrations that *Roe* was wrongly decided. The betting among many legal scholars is that Mr Roberts's respect for precedent will outweigh any personal convictions he may have about the rights or wrongs of the ruling. And nobody will publicly try to hang him because of his wife's views.

Even more important is the changing politics of abortion. The Democrats are desperate to recruit pro-life voters—particularly blue-collar voters who have traditionally voted Democratic but who have been put off by the party's strident support of abortion. Earlier this year, Hillary Clinton, the front-runner for the

Democratic presidential nomination in 2008, described abortion as “a sad, even tragic choice to many, many women”. On July 22nd, Howard Dean, the party chairman, told a group of college Democrats that their party needed to build a big tent that welcomed pro-life Democrats. The Democrats are even running a pro-life candidate, Bob Casey, against Rick Santorum in the 2006 Senate race in Pennsylvania, and he is well ahead. Will the Democrats really risk their chances of building a big-tent party—and of taking the scalp of the hated Mr Santorum—by mounting a strident attack on Mr Roberts over abortion?

Mr Roberts's Democratic critics may be on stronger ground if they focus on the commerce clause of the constitution. The clause, dry though it sounds, is a hot topic in the legal world. The constitutional legitimacy of a vast range of federal regulations depends on Congress's power to regulate interstate commerce. The Supreme Court has issued two decisions—in 1995 and 2000—that set limits to Congress's ability to intervene in non-commercial interstate matters, such as guns near schools and violence against women, in the name of the commerce clause. And many leading conservatives would like to narrow those limits still further. Janice Rogers Brown, whom George Bush has recently appointed to the federal appeals court, clearly favours a much narrower reading of the clause, and one that would sweep aside much New Deal economic regulation.

Moreover, this is one subject on which Mr Roberts, who has been on the federal bench for only two years, has left a paper trail as a judge rather than just as a government appointee. In the case of *Rancho Viejo v Norton* in 2003, he issued a dissent questioning a federal regulation to protect arroyo toads as an endangered species. He doubted that “regulating the taking of a hapless toad that, for reasons of his own, lives its entire life in California constitutes regulating ‘commerce...among the several states'.” Ted Kennedy has already argued that this opinion threatens Social Security, Medicare and the minimum wage.

The Democrats' worst nightmare

But if Mr Roberts's critics are on stronger ground here than on abortion they are unlikely to get the better of the argument. There is no clear “conservative” partly line on the commerce clause. In the recent case about medical marijuana in California, Clarence Thomas and Antonin Scalia came down on opposite sides of the fence: Mr Thomas against federal regulation on the basis of his strict interpretation of the commerce clause, and Mr Scalia in favour of the regulators on the basis of 70 years of precedent that have expanded the clause to allow the federal government to regulate a highly sophisticated economy.

Mr Roberts's opinion in *Rancho Viejo* was merely a five-paragraph dissent, and the reasoning underlying it is not evidence of judicial extremism. There is a big difference between wanting to narrow the commerce clause in the way that Janice Rogers Brown does and wanting to make sure that it is not abused to regulate almost everything, including toads.

So expect to hear at least as much about the technicalities of the commerce clause as about the morality of abortion in Mr Roberts's forthcoming Senate hearings. But don't expect his nomination to be derailed by it. Mr Roberts is the Democrats' worst nightmare—a conservative who isn't an ideologue and a youthful-looking 50-year-old who could be on the court for the next 30 years. The real question in the Senate hearings is probably not how much damage the Democrats can do to Mr Roberts, but how much they can inflict upon themselves.

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Venezuela and Latin America

Using oil to spread revolution

Jul 28th 2005 | CARACAS
From The Economist print edition

Hugo Chávez is spending some of his country's oil windfall on buying support abroad. How much of a return is he getting?

Get article background

WITH a swipe at American “imperialism” and reports on social problems in Latin America, a new regional television channel began pilot transmissions on July 24th. Telesur, backed by the governments of Argentina, Cuba, Uruguay and Venezuela, bills itself as a home-grown answer to CNN that will let Latin Americans see themselves “through their own eyes”. But 70% of the channel's $10m start-up cost comes from Venezuela's government. To many, Telesur looks like propaganda for Hugo Chávez, Venezuela's president, and his “Bolivarian” revolution, named for South America's independence hero but of increasingly socialist bent.

Predictably enough, at the urging of Connie Mack, a Florida Republican, the United States' House of Representatives greeted Telesur by approving an amendment to the Foreign Appropriations Act calling for rival propaganda broadcasts. That allowed Mr Chávez to gloat that by getting his channel on air he had “scored the first goal” against George Bush.

Telesur comes on the heels of other initiatives in which Mr Chávez is using some of his country's windfall oil revenues to procure friends and influence abroad, especially in Latin America. Thus, Venezuela has bought $538m of Argentine debt. It is talking about doing the same for Ecuador's new populist government. Venezuela has also promised to build houses in Cuba and to finance co-operatives in Argentina.

Most of the schemes involve oil. They began with a pact to expand subsidised shipments to Fidel Castro's Cuba, in return for the services of 17,000 Cuban doctors. In May, under the label of Petrosur, energy ministers from Argentina, Brazil and Venezuela agreed to develop a field in Venezuela's heavy-oil belt in the Orinoco, a refinery in Brazil's north-east, and an oil and gas venture in Argentina. In June, Venezuela set up Petrocaribe, under which it is offering 12 Caribbean countries cheap credit for oil imports. On July 22nd, at a meeting of Andean presidents, Mr Chávez proposed Petroandina, under which these oil-producing countries would co-operate on pipelines and refining.

Some of these initiatives, such as Petrocaribe, expand on the polices of previous Venezuelan governments. But now their aim is to cement an anti-American block. This goal has also led Venezuela to seek close ties with countries such as Iran and China. With Mr Castro, Mr Chávez claims to be building an alternative (called ALBA) to the Free Trade Area of the Americas, a moribund plan backed by the

United States. More immediately, oil brings Venezuela influence over a block of (mainly Caribbean) votes in international bodies.

In parallel, Mr Chávez seeks support among Latin Americans by posing as the leader of a continental revolution. At its cheekiest, this has led him to take advantage of the difficulties of Brazil's President Lula da Silva, a more moderate left-winger, to sponsor a samba school, whose theme will be *Viva la Revolución*, at next year's Rio carnival

For now, Mr Chávez's diplomacy chimes with an anti-American mood in many Latin American countries. Governments are happy to pocket Venezuelan subsidies. His willingness to meddle in their internal affairs "may cause some discomfort," says a Latin American diplomat. "But if you break publicly with Chávez you're playing Bush's game". So South American governments have ignored American pleas to shun Mr Chávez.

In its ill-tempered diplomatic battle with the United States, Venezuela has seemed to have the upper hand in other ways too. Its alliance with Cuba has subverted the American trade embargo against Mr Castro. Its refusal to collaborate with Colombia's government in its war against leftist guerrillas causes difficulties for the Americans' chief ally in the region.

Fears that Venezuela would profit from its rejection was one reason why the Bush administration lobbied so hard for the Central American Free Trade Agreement (CAFTA), narrowly passed by the House of Representatives on July 27th (see article). Donald Rumsfeld, the defence secretary, had called this "a national-security vote".

All the same, Mr Chávez's successes are fragile ones. For one thing, it is hard to see what tangible benefits Venezuelans derive from this diplomacy. Mr Chávez has alienated both of his country's main trading partners, the United States and Colombia. Oil revenues are increasingly being spent without democratic scrutiny. A once-professional diplomatic service has been turned into a branch of the revolution, its dissidents either purged or neutralised. And although the alliance with Cuba has brought new social programmes, their cost and long-term benefits are hard to determine. Despite the oil boom, unemployment officially stands at 11%.

There are also limits to the region's tolerance of *chavista* expansionism. Only Cuba has signed up for ALBA. The richer Caribbean countries are unenthusiastic about Petrocaribe. Petrosur and Petroandina feature much rhetoric and little action. Cuba apart, no other country shares Mr Chávez's distaste for representative democracy, or his disdain for regional bodies such as the Inter-American Commission on Human Rights.

In a setback for Mr Chávez, on July 27th the Inter-American Development Bank, the region's largest official lender, chose as its new president Luis Alberto Moreno, Colombia's ambassador to Washington who was discreetly backed by Mr Bush. Mr Moreno easily defeated candidates from Brazil and Venezuela.

Argentine officials have welcomed imports of fuel from Venezuela, and its help in making contacts with China, but they are cooling towards Mr Chávez. Were evidence to emerge of his hand in Bolivia's turmoil, South America would become even warier. Should Lula's troubles deny him a second term, Brazil is likely to move to the centre-right, shifting the regional balance. The death of Mr Castro, who is 78 and frail, would be a body blow to Mr Chávez. So, of course, would a fall in oil prices.

A Summit of the Americas, involving 34 countries (all except Cuba), in Argentina in November should be a pointer to the prevailing diplomatic winds. The United States wants to stop the meeting becoming a platform for Mr Chávez. But if Mr Bush turns up empty-handed (CAFTA apart), Latin Americans will continue to pay court to that generous neighbour in Caracas.

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Cuba

Summer of discontent

Jul 28th 2005 | HAVANA
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Castro battles power cuts and dissent

AFP

Onward into the twilight

FIDEL CASTRO, Cuba's Communist president, had recently promised his long-suffering people that, thanks to support from Venezuela and China, things were finally going to get better. Posters appeared proclaiming *Vamos bien!* ("we're doing well"). Yet that is not how it seems to many Cubans. Earlier this month, Hurricane Dennis ripped through the island killing 16, the highest toll from such a storm in decades. Over the past fortnight, eight children have died in Havana from illnesses believed to be caused by deteriorating hygiene.

For Cubans, these look like signs that they are slipping into the mire of underdevelopment which they had escaped through massive subsidies from the Soviet Union before its demise in 1991. Since then, the island's infrastructure has received little investment. The result this summer: daily power cuts of up to 18 hours; a water system that leaks more than it delivers; dilapidated and overcrowded homes; cratered roads and scarce public transport; and growing weaknesses in the much-vaunted health and education systems, not to speak of a shortage of insect repellent with which to battle mosquitoes.

Patience is again wearing thin, as it did in the early 1990s. There have been spontaneous protests over power and water shortages. At night, anti-Castro graffiti appear and stones and bottles fly in blacked-out streets. So far, these incidents have been small and local.

Cuba's tiny, divided and repressed dissident movement is trying to take advantage. It has staged several almost unprecedented street demonstrations in Havana this month. They have been squashed: the regime has quickly mobilised larger groups of loyalists to shout down the dissidents. Some 30 opposition members were arrested, though most were soon released.

Mr Castro insisted all was well in a speech on July 26th, a holiday marking the start of his revolution. He claimed that Cuba's economy would grow by 9% this year, despite the black-outs and a 40% fall in sugar production. He promised to end the power cuts within a year, to build 100,000 new homes next year, and said that Chinese buses and railway locomotives were on the way. Maybe. But in their current mood, Cubans want more than promises.

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Peru

Fujimori dreams

Jul 28th 2005 | LIMA
From The Economist print edition

A fugitive plots his return

Reuters

Of Japan, perhaps

IT MIGHT have been a special day for Alberto Fujimori: July 28th was not only his 67th birthday but the date when he once expected to end a third consecutive term as Peru's president. Instead, he lives in Tokyo, having resigned by fax as his regime crumbled in November 2000. But Mr Fujimori claims that he will soon return to Peru to run in a presidential election in April 2006.

He has launched a new political party called Sí, Cumple ("Yes, he delivers"), renewed his Peruvian voter-identification card and broadcasts a weekly radio programme. On July 22nd, via a television link, he addressed a rally of supporters in Lima. In a crowded field of possible candidates, he tops some polls with up to 23%.

His supporters recall that in his decade in power, Mr Fujimori vanquished the Maoist Shining Path guerrillas and set Peru on a path of episodic economic growth. But he also presided over racketeering and abuse of power. Many of his top collaborators, including Vladimiro Montesinos, his spy chief, are in jail. Prosecutors estimate that $1.8 billion was stolen from the state during his tenure. Mr Fujimori claims, lamely, that he knew nothing of all this.

While one recent poll found that one respondent in two believed that Mr Fujimori will return, this seems unlikely. Congress banned him from holding public office for ten years, until 2011. To achieve a third term—which violated the constitution—Mr Fujimori first packed the constitutional court and then rigged an election in 2000. He faces 22 charges including fraud, kidnapping, murder and organised crime, and is the subject of an Interpol arrest warrant. Peru has filed two requests for his extradition. But Mr Fujimori claims Japanese as well as Peruvian nationality. Japan has made it clear that it does not extradite its own nationals. Peru is mulling whether to take the case to international tribunals.

Mr Fujimori claims to be undeterred. He says he is the victim of political persecution, and points out that investigators have yet to find secret bank accounts in his name. He has two things on his side. One is judicial torpor: of 335 criminal cases relating to his administration, sentence has been passed in only 39. Because of the delay, several defendants have been released. Anti-corruption prosecutors are running out of money and fear that they are losing the battle.

The second factor is the alleged peccadillos of the government of Alejandro Toledo, who was elected as Peru's president in 2001. These are on a far smaller scale than those of Mr Fujimori's administration. But in a survey this month by Apoyo, a polling firm, 56% said that corruption is the most serious problem in Peru. Mr Toledo seems to have lost much of his former zeal for fighting graft.

This means that Mr Fujimori's allies may increase their presence in the country's Congress next year. In future, perhaps, they could manoeuvre to get the charges against their chief dropped. Until then, it is hard to imagine that Mr Fujimori's plans for a political comeback are anything more than a dream—or for many Peruvians, a nightmare.

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Brazil

Lion's share

Jul 28th 2005 | RIO DE JANEIRO
From The Economist print edition

A tax revolt against a spendthrift state

EARLIER this month, some 200 federal police swooped on Daslu, a bejewelled São Paulo high-fashion mall. In front of television cameras, they seized merchandise and dragged the owners off to jail on suspicion of tax fraud. Normally, Daslu's fate might evoke little sympathy: it is a monument to mammon where the extravagant gather even in the worst of times. But some Brazilians have wondered aloud about the government's priorities.

In many Latin American countries, governments are too poor to provide basic services. Not in Brazil: its tax revenues now account for 37% of GDP, a figure similar to that in the United States and twice as high as in Chile. Even so, evaded taxes are estimated to amount to a further 11% of GDP. Brazilians refer to the tax authority as the “lion”. Its voracious feeding habits can be observed in the wilds of São Paulo's financial district, where a giant screen keeps track of how much money taxpayers have fed it this year (over $165 billion so far).

With more than 55,000 articles and 63 separate levies, the Brazilian tax code is a monster. CPMF, ICMS, PIS, COFINS—the acronyms of different taxes scroll across the newspapers like cryptograms. Armies of lawyers are deployed to decipher them. There are taxes on top of taxes, a fiscal “waterfall” that can drown business or flush it underground. Some 3m Brazilian businesses are currently in tax arrears.

Citizens are starting to bite back. In May, a “Brazilian Front” for tax reform took to the streets. It forced the government of President Luiz Inácio Lula da Silva to scrap planned new taxes which, it claimed, might have endangered 100,000 service jobs. Earlier this month, the front took aim at a decree which eases export taxes but leaves tax deadlines unaltered. While businesses need an average of 57 days to collect on sales, taxes are due within 25.

For the past decade, Congress has tinkered with taxes while jibbing at proposals for a thoroughgoing overhaul. Prospects for reform look bleak: Lula's government has been disabled by corruption allegations surrounding the ruling Workers' Party (PT). Yet paradoxically, the scandal may focus more attention on the tax burden.

Leaders of the PT are accused of using public funds to buy the loyalty of legislators from allied parties (they deny that, but admit taking undeclared loans to finance campaigns). The tax rebels see a compelling link between pilfering in Brasília and the state's insatiable appetite for revenue. Though Lula has won praise from investors for honouring Brazil's public debt, critics point out that he has done so not by cutting other spending but by collecting record levels of tax.

According to Roberto Fendt, an economist specialising in public accounts, the government has become too big and too powerful for its own good. “The concentration of power creates a sensation of impunity,” he says. “People at the top act as if they will never be punished.” Time, perhaps, for the lion to go on a diet.

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Canada

Embarras de la richesse culturelle

Jul 28th 2005 | MONTREAL
From The Economist print edition

Luvvies squabble for sated punters

ITS boosters describe Montreal as a “city of festivals”. They do not exaggerate: almost every day of the year is devoted to celebrating one thing or another—or three or four during the summer. June alone saw festivals of techno, jazz, chamber, reggae, baroque, and “liberation” music. The non-musical could choose from contemporary and fringe theatre, native peoples' culture, street art, bicycles, fireworks and, thankfully, beer.

These cultural bashes create hundreds of jobs. The larger events pull in up to C$75m ($60m), much of it from visitors. That is valued in Montreal, whose economy has lagged that of Canada's other big cities. But some Montrealers now complain of festival fatigue—an ailment soon to be aggravated by a proliferation of film festivals.

Last year, a federal arts body and its provincial counterpart in Quebec halted funding of Montreal's World Film Festival (MWFF). This had been long since eclipsed by a rival in Toronto. Instead, the cash has gone to a new film fest launched by Équipe Spectra, the organiser of Montreal's successful jazz festival. The MWFF's secretive president, Serge Losique, threatens to carry on alone. Meanwhile, Spectra has fallen out with the organisers of a festival of independent film. All three events are scrapping over films and stars.

Behind this battle lies a cultural clash. Most Montreal festivals are organised by enthusiastic volunteers. Spectra is a professional business. Many of the smaller events feel threatened by it.

Some Montrealers question Spectra's finances: each of its festivals is a non-profit company, allowing them to derive part of their budget from state funding. But each event also buys services from the private holding company, which is controlled by many of the same people. Spectra's network of concert halls, production companies, artist-management and ticket-selling services all profit similarly. “Spectra is about business development, not cultural development,” sniffs a rival organiser.

Alain Simard, Spectra's boss, retorts that his firm is a “capitalist co-operative” and laughs at claims that it is making anyone rich. Funding bodies scrutinise its books. He has turned down lucrative invitations to set up similar jazz festivals from Paris to Beijing. Whatever the gripes of the purists, jaded Montrealers will doubtless applaud if Mr Simard's businesslike approach creates a second world-class cultural event in their city.

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Egypt

The bombers stir a toxic brew

Jul 28th 2005 | CAIRO AND SHARM EL-SHEIKH
From The Economist print edition

Reuters

Will the bombs that killed scores of Egyptians and foreigners in a holiday resort make it harder for President Hosni Mubarak to loosen up his country's politics?

THE suicide bombs that killed at least 67 people (hospitals put the toll at 88-plus) on July 23rd in the Red Sea resort of Sharm el-Sheikh seem, so far, to have been homegrown—or, at least, to have been carried out by locals, though several groups, one with a proclaimed link to al-Qaeda, did claim to have done the deed.

Four days later, the state news agency announced that Egypt's 77-year-old president, Hosni Mubarak, would stand for a fifth six-year term of office, in an election on September 7th. A parliamentary one is to be held in November. Under the prodding of America, Mr Mubarak says he will give Egyptians more political freedom. For the first time in 24 years, the president will face at least one rival candidate. But the bombings are hardly likely to make Mr Mubarak free things up faster.

Though his government at first suggested that the attacks might have been orchestrated from abroad, suspicion soon turned to a network among the bedouin of northern Sinai. They would have had the best opportunity to make such an attack. And they had a motive.

One of the three suicide-bombers rammed a pickup truck into the lobby of one of Sharm el-Sheikh's tourist hotels; the other two, one in a car and the other on foot, were stopped at checkpoints but managed to detonate their explosives. The death toll outstrips the 62 people killed in Luxor in 1997 and the 34 killed last October in two other Red Sea resorts, Taba and Ras Shaitan. The bedouin network was blamed for last year's attacks too.

Egyptian investigators say that DNA tests on the body of one of the bombers proves he was the brother of a fugitive wanted for the Taba attack, after which the authorities arrested up to 3,000 bedouin, many of whom claim to have been tortured. The police are still hunting for others in the mountains.

Locals say the bedouin would know the paths through the Sinai peninsula's twisting ridges and wadis, routes that would be taken if a lot of explosives were to be slipped past the many checkpoints on bigger roads. For decades, many bedouin, working away at growing drugs in the valleys or smuggling illegal Russian migrants into Israel, have dodged or bribed the security forces. Many are harassed by the police. Some resent their relative poverty while fat-cat developers, some in cahoots with Egypt's army elite, make fortunes out of the prime beach and diving sites along the peninsula's coast.

But this does not rule out the possibility that the bedouin have contacts abroad and may co-operate with an international terrorist movement; the ringleader of the Taba attack was reportedly a Palestinian. A credible claim of responsibility for the recent bombings was in the name of the “Abdullah Azzam

Brigades of al-Qaeda in Egypt and the Levant", which also said it carried out the Taba bombings.

The statement suggested a mix of motives: vengeance for Palestine, Iraq and Chechnya, as well as anger against Egypt's government for persecuting the "martyrs of Sinai" after the Taba attacks. Still, there is little to suggest that the network extends beyond a handful of families, though the radicalisation of even a few of Sinai's bedouin, who live on the edge of one of Egypt's main tourism zones, is frightening.

Tourism, Egypt's main source of revenue, has been taking terrorist blows every four years or so—and has always bounced back. More worryingly for Mr Mubarak, this time the terrorists hit a town that he has personally adopted as a symbol of what he thinks his regime does well: development and diplomacy. The president had turned his "Red Sea riviera" into a showpiece of broad, clean streets and top-class resorts. It was also a diplomatic capital, where he has hosted international summits and had bigwigs to stay.

Throughout the 1990s, Mr Mubarak has justified his hold on power, and the draconian emergency laws underpinning it, by his need to fight terrorism and keep violent Islamists at bay. But some Egyptians have been quick to say that the attacks merely highlight his regime's incompetence.

Several parties, including the left-wing Tagammu and the Nasserists, say they will boycott the elections because they are sure to be unfairly run. The Kifaya (Enough!) movement never proposed a candidate. Constitutional obstacles have made it hard for a serious Islamist contestant (for instance, an independent backed by the Muslim Brotherhood) to stand. Only Ayman Nour, leader of the liberal Ghad (Tomorrow) party, is still in the fray. Bombs or not, Mr Mubarak looks set to hold on to power. Still, politics in the next few months should be livelier than before.

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Muslim theology

Coming together

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The men of learning against the men of violence

OVER the few days before the attack on London of July 7th, something historic was happening in the world of Muslim theology. After some careful deliberations in the air-conditioned comfort of a hotel in Jordan's capital, Amman, the world's leading Muslim scholars—over 170 of them from 35-odd countries—made a series of pronouncements designed to affirm their own authority, soften differences and deal a blow to advocates of terror.

The things these august gentlemen decided on may sound arcane to non-Muslims. But for the hosts, including Jordan's King Abdullah, the agreement was an encouraging first success in what will have to be a long ideological war against readings of Islam that lend support to violence.

In several ways, the muftis and professors agreed to minimise their own (previously sharp) differences and work together to promote what they regard as "good theology" over some superficial, violence-promoting interpretations of Islam that have circulated, electronically and in print, all over the world. Among the scholars' main conclusions is that nobody who accepts Islam's basic beliefs should be denied the label of Muslim. A statement of the obvious? Far from it, because a hallmark of virtually all the shrillest voices in Islam is that they reject the Muslim credentials of anybody who disagrees with them. As an example of a Muslim thinker who rejects anybody less extreme than himself as an apostate, many would cite Ayman al-Zawahiri, an Egyptian who is one of the leaders of al-Qaeda.

Equally important, the scholars announced a sort of "mutual recognition" agreement between Islam's eight main schools of legal interpretation: four Sunni ones, the two main Shia traditions, the Ibadis of Oman and the small but prestigious Zahiri school. While these schools' leaders will never concur on everything, they recognised each other's authority in their respective communities—and resolved to deny authority to anybody who purports to be a scholar but lacks the training.

At least in theory, this implies a degree of mutual respect between rival versions of Islam that has not been seen since the Fatimid empire a millennium ago. More practically, the pronouncement should act as a restraining influence in Iraq, by denying Sunni Muslims any right to attack their Shia compatriots as heretics.

As an instance of bad theology being used to ignoble ends, many scholars cite the notorious *fatwa*, or religious ruling, issued in 1998 by Osama bin Laden and his comrades from Egypt, Pakistan and Bangladesh. It cited some of the gorier lines from the Koran—"slay the pagans wherever you find them, seize them, beleaguer them, lie in wait for them with every stratagem"—to justify attacks on "Crusaders" (ie, westerners) and Jews. More traditional readings of the Koran would argue that these lines refer to a specific situation—when the Prophet and his companions faced a surprise attack from adversaries who had torn up a treaty—while the more emollient passages of the Koran, urging tolerance, state a more general rule. The precise meaning of the Koran's so-called "sword verses" is hard to discern. But moderate scholars make a plausible case when they argue that only well-grounded theology can cure the effects of the bad, extremist kind.

Still, how much will the Amman decisions resonate with ordinary believers in the so-called Arab street, where many may still be more impressed by al-Qaeda's spectacular actions than the careful thoughts of the greybeards? A lot, insists Abdallah Schleifer of Cairo's American University. "The ordinary Egyptian is troubled by the sight of Sunni Muslim fighting Shia Muslim in Iraq, and this will help to clarify his thinking," he says. "It will also be a blow against the bad effects of store-front religion—extremism spread by ignorant, self-appointed preachers."

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Mali

And still they starve

Jul 28th 2005 | TIMBUKTU
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Another Saharan country is in dire straits through no fault of its own

A DROUGHT had already scorched the southern edge of the Sahara desert before locusts burst out of the oases around Kidal in Mali last year, settling on cereal crops there and nearby in even more destitute Niger. As a result of a meagre harvest, the cost of millet went up by 30%, sorghum by 50% and maize 60%. In both countries, state and village granaries are low or empty. Officials in Mali's capital, Bamako, reckon that more than 4m in the two countries risk starvation, 1.1m of them in Mali.

The damage locusts did to the scrub grasses on which livestock depend has been even more devastating. Hundreds of herdsmen and tens of thousands of cattle have withered and died on futile treks in search of pasture. Survivors in Mali, whose population is 11m, have gathered in unusually large numbers in the Gourma region, east of Timbuktu, raising tensions there and overgrazing land that, but for the Niger river that sweeps slow and brown in a life-giving arc through Mali, would already be desert. Mali's 1.7m nomads, already among the poorest in the world, have been particularly hard hit. They used to trade a goat for a sack of millet, which now costs four goats.

Mali's minister of finance, Abou Bakar Traoré, can only shake his head sadly. His country is the fourth-poorest in the world, according to the UN, and getting poorer. Brought in from the private sector and with a clean reputation so far, Mr Traoré does not know what to make of promises made at the meeting of the eight rich countries' leaders at Gleneagles in Scotland earlier this month. “I haven't seen anything about debt relief,” he says. “Not a single piece of paper.”

Mali is still paying interest on its debts. Even if they were forgiven, Mr Traoré thinks the benefits would be offset by the high oil price and low price of cotton, Mali's main export. Transport costs in his landlocked country have risen by 15%-plus due to higher fuel costs; civil war in Côte d'Ivoire, to the south, has further raised costs since it has blocked off the route to Abidjan, the usual port for Malian trade. Road and rail links west to Dakar, in Senegal, are ropy, so Mali's lorry drivers face a grinding round trip of 2,000km (1,200 miles) or more through Benin or Togo to get any goods on to the world market.

There are some positives. Mali is run better than most other countries in the region. The European Union, a big donor, likes President Amadou Toumani Touré. A former general who introduced multi-party democracy in 1992 after seizing power in a coup and then stayed out of politics for a decade

afterwards, he is still fairly popular, since he seems keener on the welfare of his people than on filling his own wallet. Bamako, sleepy but safe and fairly well run, looks nothing like the capital of the fourth-poorest country in the world. For all the challenges of isolation, drought and famine, the country is peaceful and socially cohesive. Marriage across Mali's tribes is quite common. Except in its desert areas, civil strife is rare.

That may be the country's strongest, and perhaps only, card. As a moderate Muslim country, Mali could have a useful role in helping to find and close down Islamist terrorist camps in the Sahara. Its army is playing its part in a Pentagon Trans-Sahara plan, to be funded with $500m over seven years, to train some 3,000 African commandos for desert and border operations and to link forces in various countries with secure satellite communications. Algeria, Chad, Mauritania, Niger, Nigeria, Morocco, Senegal and Tunisia are also involved, with Libya perhaps to be added if its relations with the United States improve. Mali hopes that helping to catch terrorists might shame America's administration into slashing the subsidy of $3 billion or so it gives its own cotton growers (many of them Texan) and which helps keeps Mali (and Niger) so poor.

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Madagascar

Getting stoned

Jul 28th 2005 | ANTSIRABE
From The Economist print edition

Madagascar must try to reap more of a benefit from its plentiful gemstones

THESE days the vast swathes of brick dirt that gives Madagascar its nickname “the Red Island” are pockmarked by small holes: evidence of the search for sapphires, rubies and other precious stones. Mining accounts for 3% of the country's GDP and 1% of its export revenues, and provides 500,000 seasonal and full-time jobs in a population of about 18m. But if the government improves the miners' and cutters' skills and curbs smuggling and corruption, the Malgaches would benefit a lot more.

Since the discovery of blue sapphires in 1998, boom towns have been springing up on the savannah, luring tens of thousands of miners, prospectors and dealers. But in many ways it is a classic African story of a resource-rich country—with the largest reserves of sapphires on earth—that remains one of the world's poorest. Still, the World Bank hopes that, properly managed, the industry may yield more benefits to ordinary people than elsewhere in Africa, and perhaps bring in as much as $400m a year.

So the Bank and the government have set up the Mineral Resources Governance Project. It teaches diggers and small traders basic gemology and pricing and trains advanced students to become licensed cutters, so helping local Malgaches to get higher prices for their cut stones and compete against the Thais, who dominate the sapphire market. It may also reduce smuggling.

Until last February, a foreign gem trader had to get his business incorporated in Madagascar in order to export stones. Many traders and jewellers ignored this rule, sometimes sewing gems wrapped in plastic into their underwear to avoid scrutiny at customs. Others simply bribe customs officials. Now the government has abolished the need for in-country incorporation and has eliminated the export tax on cut stones, but will tax rough ones at 2% for export.

Will that reduce illegal trade? An anti-corruption body estimates that 50kg of rough sapphires are smuggled to Thailand every week; a good 90% of people in the mining sector, especially those in authority, are reckoned to be bent. Madagascar's second national convention on fighting corruption has just ended. Delegates said the clean-up must include mining. They have their work cut out.

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Zimbabwe

Cash, please

Jul 28th 2005 | JOHANNESBURG
From The Economist print edition

Robert Mugabe begs his friends to bail him out. They probably will

CRIPPLED by shortages of fuel and food, Zimbabwe is going from bad to worse. This time President Robert Mugabe may be finding it harder than usual to borrow money and fend off international censure. His country faces expulsion from the IMF if it proves unable to service its debt. And the UN's special envoy, Anna Tibaijuka, says that the recent demolition of urban homes and black-market shops, leaving some 700,000 people without shelter or livelihood, has created a humanitarian crisis. The UN's World Food Programme says that 2.9m of Zimbabwe's 11m people face starvation unless they get handouts. The United States and Britain, Mr Mugabe's loudest critics, now want Zimbabwe's travails debated in the UN Security Council—with the prospect of Mr Mugabe being put, for the first time, in the UN's dock.

South Africa, already reportedly owed some $50m for unpaid electricity, telecom and fuel bills, is pondering whether to lend cash to cover part of the $290m arrears that were due to be paid this week to the IMF. President Thabo Mbeki has been berated in the West for his hitherto ineffective policy of "quiet diplomacy". But although African leaders across the continent are still loth to criticise Mr Mugabe in public, a shift may be taking place. Mr Mbeki may insist that Mr Mugabe should not get a loan from South Africa unless he starts negotiating with the opposition Movement for Democratic Change (MDC) and imposes at least a semblance of economic discipline. Olusegun Obasanjo, Nigeria's president and the African Union's current chairman, has also asked Joaquim Chissano, Mozambique's ex-president, to talk some sense into Mr Mugabe.

Even if conditions are made, it will be hard to ensure that Mr Mugabe meets them. Greg Mills of the Brenthurst Foundation, a South African think-tank, says that lending Mr Mugabe the cash would be like giving a drug addict a fix. Mr Mbeki is in the uncomfortable position of trying to coax Zimbabwe towards reform while knowing that, if South Africa refuses to help out, it could melt down completely.

Mr Mugabe, for his part, is hedging his bets. This week in China he sealed a deal for economic and technical co-operation, though it is unclear how much actual cash that will provide. What it may mean, however, is that China would veto a censorious resolution on Zimbabwe in the UN Security Council.

In the meantime, Zimbabwe's political landscape is getting fuzzier. There are rumblings of discord within both main parties. The MDC, after years of repression and a dodgy election in March that gave the ruling ZANU-PF two-thirds of parliament's elected seats, is running out of ideas. It hasfailed to mobilise mass demonstrations or mass stay-aways. Roy Bennett, a former MP for the MDC recently freed from jail, says his party has been hijacked by "corrupt opportunists". A power struggle between Morgan Tsvangirai, its president, and Welshman Ncube, its secretary-general, is said to be crippling the movement.

ZANU-PF has been weakened too, by ethnic divisions and power struggles for the succession. But party dissidents do not, so far, have much support. The gravy train is likely to keep most ZANU-PF people on board. And if Mr Mbeki and the Chinese both come up with the cash, Mr Mugabe could survive for quite a while yet.

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AIDS in China

Anatomy of an epidemic

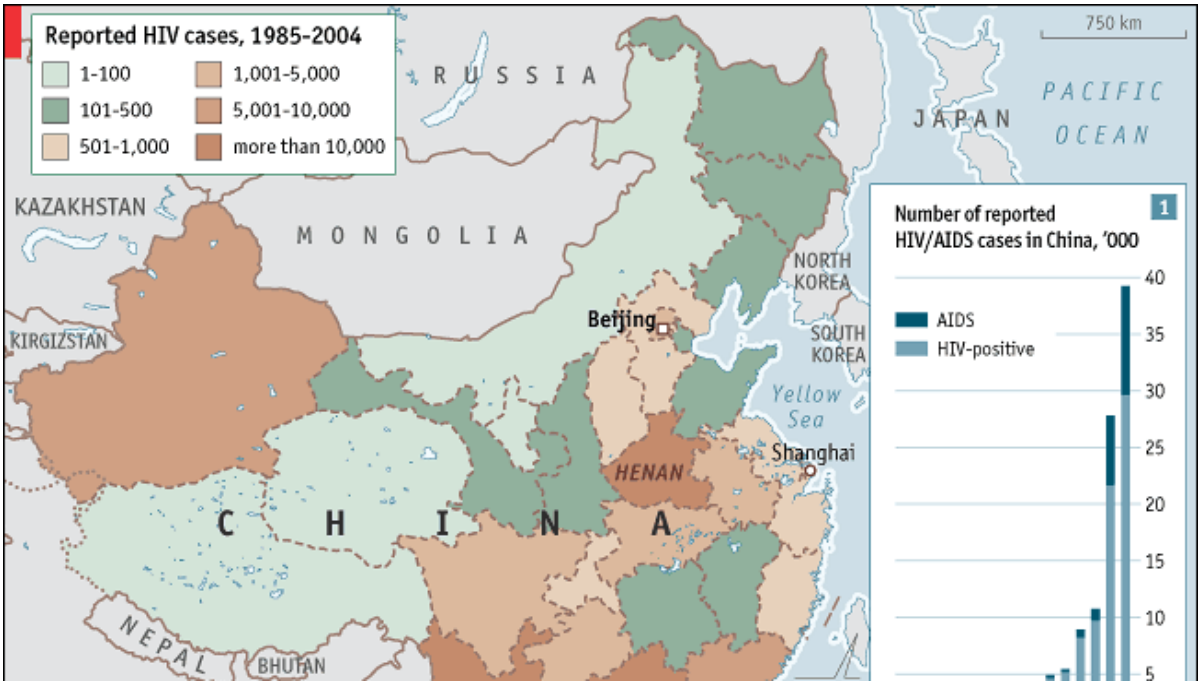
Jul 28th 2005 | RUILI
From The Economist print edition

AFP

It is not too late to avert a national catastrophe

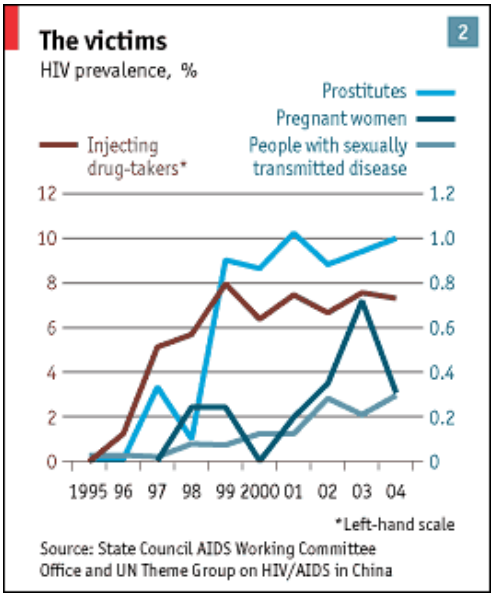
Get article background

SURELY China does not face a general AIDS epidemic? The government says that only 0.07% of the general population is infected with HIV, the virus that causes AIDS, and, unlike some other governments' figures, this one may be an overestimate. The World Health Organisation (WHO) would prefer to quote a range of 0.05-0.08%. Moreover, large areas of the country have relatively few cases of HIV: in only three of China's 31 provinces, autonomous regions and municipalities are more than 10,000 people infected. Even so, China does have an AIDS epidemic and, though it may not yet be a catastrophe on a national scale, it has the potential to become one.



Several features of this epidemic are already serious enough to cause grave concern. First, it has spread to every province (see map) and half the counties within them. Second, the number of reported cases is growing (chart 1, with map) and, since 85% of those infected do not know they are HIV-positive, the growth will continue. Third, among certain groups, the infection is present in alarming proportions (chart 2). Fourth, even a low prevalence rate, such as the WHO's bottom-of-the-range 0.05%, means 650,000 infections; the government's rate translates into 840,000. Either means personal tragedy on a vast scale. This points to the fifth reason for concern: in a country as big as China, an AIDS explosion would have economic, political and social consequences for the entire world.

Such an explosion, however, is far from inevitable, thanks mainly, and paradoxically, to another nasty disease, SARS. For 15 years or more after China announced its first AIDS-related death in 1985, the country's leaders were in denial about HIV. Few cases were reported, and homosexuality and promiscuity, the two agents by which this “western” affliction was presumed to spread, were said to be limited in China. Then, in November 2002, came the outbreak of severe acute respiratory syndrome, SARS, in Guangdong province. By the time it had been contained, China's leaders had come to realise just how vulnerable the country was to such a plague. SARS was not like a nasty new strain of flu that carried off great quantities of sickly people and then was gone. It was a deadly and highly contagious disease that threatened to paralyse China and did indeed bring Beijing to a standstill, with even the leaders' Zhongnanhai compound being quarantined. The economic threat posed by such diseases was clear, and suddenly AIDS too looked potent.



By that time, however, the disease was well established among two large groups. One was chiefly made up of peasants in central China, people so poor that in the late 1980s and early 1990s they readily and regularly sold their blood to dealers known as bloodheads. The trade was vastly profitable in a country with a huge need for blood and no tradition of giving it.

In some places, almost everyone was bringing blood to the market; collection points were often set up in fields. But the onset of anaemia soon put a limit on the amount that sellers could provide. Not for long: by 1993 the bloodheads realised that they could both keep anaemia at bay and harvest an almost perpetual crop if they took only plasma. To cut costs, they mixed together the blood of all the peasants of the same group before extracting the plasma. They then separated the plasma and transfused the remaining blood corpuscles back to the peasants. No surer way of spreading hepatitis-B, hepatitis-C, malaria and HIV could be imagined, especially as many blood-sellers went from one collection point to the next.

More people in China have contracted AIDS through the sale of blood—the equipment used was usually unsterilised—than through any other means. In Henan province alone, according to a recent report, about 300,000 people became infected, mostly in 1994-96. Roughly 170,000 people contracted HIV through the sale of plasma, the other 130,000 through the use of dirty syringes in the collection of whole blood, or by getting it through transfusion.

The sale of blood was made illegal in 1998 and steps have now been taken to improve the entire blood-donation service and to reduce the number of collection organisations—crucial to establishing quality control—from over 600 to about 350. But 350 is still far too many, and they remain commercial ventures, belonging to hospitals or laboratories, even though no one is meant to be paid for giving blood (some sales probably continue). Moreover, no one has ever been brought to book for what is widely acknowledged to be a national scandal. It remains a matter of great political sensitivity.

Drugs and sex on the border

As a means of transmitting HIV, however, commercial blood-gathering has been overtaken by dirty needles among drug-takers (chart 3). The resulting outbreak has been growing for years, especially in the southern provinces that abut the drug-producing countries of Myanmar, Laos and Vietnam. By 1993, one of these, Yunnan, had more AIDS cases than any other part of China. Hence the decision that same year to open the country's first AIDS hospital there, in Ruili, the most AIDS-ridden town in the province.

Despite a large general hospital in the middle of the town, and on the other side of the road an AIDS centre for women and children started in 2001 by Britain's Save the Children charity, there is no sign of an AIDS hospital in Ruili today. The need, however, is greater than ever.

Ruili stands on the border with Myanmar, which provides a constant supply of drugs. Also pouring over the border are the Burmese prostitutes who work in the salons and massage parlours close to the lorry park by the crossing-point. These girls are poor, and cheap; some earn as little as 5 yuan (about 60 cents) per customer. Many carry sexually transmitted diseases, and some are HIV-positive. They may have read the sign by the frontier post that shows a tightly furled condom, held in a delicate female hand, with a message recommending its use for health, happiness and protection against AIDS, but the girls are often too poor, or too intimidated, to refuse a client, often a truck-driver, who insists on unprotected sex.

In Thailand, which has also been threatened by AIDS, the brothels proved to be a useful element in the successful fight to avert a general epidemic. Most brothel-owners readily agreed to the use of condoms, as did the women working in them. To an extent, Ruili offers hope of a Thai outcome. The Chinese prostitutes in the town—many of them members of minority groups such as the Dai, Jingpo, De'An and Lisu, who make up about 60% of the local population—are likely to work for madams who look after their girls and favour condoms. And though prostitution is illegal, despite its undisguised practice all over the country, the madams do not object to efforts to inform their girls and provide them with condoms.

Moreover, Chinese prostitutes are unusual in that most of them are free agents. They are typically village girls who, like so many in today's China, want to make money fast. With little education, they see prostitution as a way to do this, before they settle down, marry and have children, perhaps with a small business. Uneducated they may be, but they are independent enough to take advantage of both advice and prophylactics, if available.

Burmese prostitutes are different. They are much less likely to be girls with a business plan, much more likely to be those who have fallen on hard times and are therefore vulnerable to the exploitation of pimps. In China, they are also, as foreigners, ineligible for free treatment. Once infected, they can, of course, pass on their infection to anyone.

Drug-addiction is a further complication, and one that may afflict any of Ruili's prostitutes. The Dai have been taking opium for years, and for some Dai men drug-taking is seen as a rite of passage. Among other Chinese, to be visibly under the influence of drugs may be a sign of affluence. So drugs are popular on both sides of the border. Needles, though, are not—and one shot with a dirty needle is enough to ensure infection.

Ruili, you may say, is untypical, both because of its palm-fringed boulevards, Buddhist temple and Christian church and because of its louche atmosphere, minority traditions and proximity to Myanmar. Yet if its drugs and prostitutes also make it untypical, that is only because they are a bit more obviously available here than in other parts of China. A plausible estimate puts the number of Chinese drug-takers at over 1m, and prostitution is now conspicuously practised in every city, close to almost every hotel, every building site and even every mine, where tented bordellos appear as soon as the first sod is turned.

The Chinese, it should be said, are probably no more promiscuous than any other nation. Indeed, their culture has long frowned on extra-marital sex, and so has the Communist Party, so much so in the 1980s that all signs of commercial vice were ruthlessly suppressed, with the happy result that sexually transmitted diseases were all but stamped out. Now, however, they are back, and flourishing in particular among the members of another new phenomenon—the “floating” population of 120m-140m people who have left a poverty-stricken existence in the countryside for menial jobs in the cities.

Some say most building workers are too tired and too poor to patronise prostitutes. But most of those who make it their business to worry about AIDS in China see these migrants as a terrifying transmission belt for HIV. Removed from their families for most of the year, they occasionally go home for a holiday, perhaps bringing an infection with them. Meanwhile, the 400,000 truckers who pass through Ruili each year are also plying back and forth, some taking AIDS to a wife or girlfriend.

The huge task now in China is to contain the two main AIDS outbreaks. The blood-borne one is waning, though it leaves a terrible legacy of infected people. The drug-driven one is growing, and threatens to spread through heterosexual sex. Encouragingly, the SARS-struck government has changed its attitude dramatically. Whereas a few years ago a woman carrying a condom was liable to be arrested as a prostitute, condoms are now officially promoted and even, in theory, given away. In Yunnan, hotels have to provide them (for a price) in their guestrooms.

Treatment is also improving. Since December 2003, the “four frees and one care” policy has been in force. This brings free anti-retroviral drugs to all infected people in the countryside and to poor people in towns; free advice and testing for those who want it; free drugs for infected pregnant women, to prevent mothers infecting their babies during childbirth; free schooling for AIDS orphans; and financial help for the families of people affected by HIV.

Into battle, at last

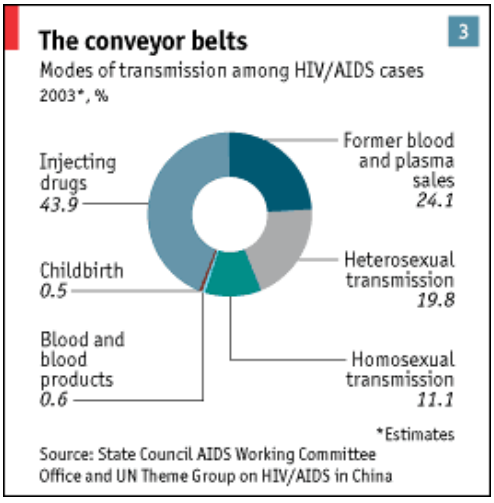
Getty Images

What hope for her?

The policy was announced by the prime minister, Wen Jiabao, when visiting AIDS patients in Ditan hospital in Beijing. Both the policy and the visit were an overdue acknowledgment that AIDS demanded a decent government response, and that those who suffered from it should not be treated as pariahs. The government is trying to gather more information about the epidemic. It is spending more: the budget for 2004 of 810m yuan ($98m) was over twice the budget for 2003. It is doing more to promote education and awareness. And it has brought in a requirement that all local officials should be regularly assessed on their efforts to combat AIDS.

Perhaps more bravely, it has also started to tackle the problem of drug addiction by means other than its traditional response of retribution and re-education. Needle-exchange programmes have been introduced in about 50 places in the south and north-west, and efforts are at last being made at some centres—perhaps 100 by the end of this year—to use methadone to wean addicts off drugs. The trouble is that in order to prevent methadone treatment being seen as a soft option, it is available only to people who have been jailed three times for drug offences. Anyone meeting that criterion will have been taking drugs for at least five or six years, and will therefore probably be thoroughly hooked and have shared hundreds of needles.

A bigger difficulty is the scale of the measures being taken, and the zeal or inertia with which they are implemented. Foreign AIDS experts speak approvingly of many of the Chinese officials who are engaged in the struggle against the disease. But, in a country with 80,000 people suffering from full-blown AIDS, they are pitifully few. Only three hospitals in Beijing take AIDS patients, for instance, and Ditan, the main one, has treated no more than 400 or so as in-patients and another 700 as out-patients since its first case in 1987. China as a whole has only 50 AIDS doctors, and only about 15,000 people are being treated with anti-retroviral drugs.


The conveyor belts
3
Modes of transmission among HIV/AIDS cases
2003*, %
Injecting drugs 43.9
Former blood and plasma sales 24.1
Childbirth 0.5
Heterosexual transmission 19.8
Blood and blood products 0.6
Homosexual transmission 11.1
*Estimates
Source: State Council AIDS Working Committee Office and UN Theme Group on HIV/AIDS in China

Beyond Beijing, the energy with which the government's policies are executed varies. China is vast and decentralised, and clear orders from the centre may reach the provinces as confused murmurs. If all China's mass organisations, including the party, the women's federation and the youth league, were truly mobilised, then the “people's war” necessary to fight the epidemic could be successfully waged. But the leadership seems reluctant. And, despite its clear concern about AIDS, old habits of repression and secrecy often reassert themselves when, for instance, gay websites offer information about AIDS.

Even so, some independent groups are trying to fill the gaps. The Mangrove Support Group is one, which promotes knowledge and offers care in five provinces, as well as via the internet. Over 30 groups offer assistance to homosexuals, and a few others like the Positive Art Workshop in Beijing offer help and therapy. In general, though, such groups are rare, as are any

non-governmental organisations—a problem for the Global Fund, the partnership conceived at the G8 summit in 2000 to fight AIDS, TB and malaria: a share of its cash is meant to be spent through NGOs.

If China is to contain its AIDS epidemic, it will need help, lots of it, from international agencies and from NGOs. AIDS everywhere presents a range of problems that are not susceptible to solution by a single agency. One big task, for example, is that of giving information. Many Chinese are still deeply ignorant about AIDS. The stigma attached to the disease is potent, despite widespread sympathy for the peasants of Henan, and despite the efforts of a few brave people like Pu Cunxin, one of China's best known actors, who campaigns tirelessly against prejudice.

A very different problem concerns treatment. China produces only five anti-retroviral drugs with which to concoct treatments for HIV-positive people. The Clinton Foundation is helping, but more drugs are needed for those who find these “first-line” ones do not work, or work only with intolerable side effects. No special drugs for children are available at all.

Another particularly acute problem concerns gay men, most of whom in China are married. Although homosexuality is no longer regarded as a psychiatric disorder, convention and economic security in old age combine to make marriage a desirable choice for nearly all men. Few are therefore openly gay, though they may well gather in certain bars, clubs or parks to arrange sexual assignations. If they become infected—some say 1-5% of China's 10m-20m homosexuals are HIV-positive—they will probably also infect their wives.

The troubles do not stop there. How do you promote the use of condoms in a society that prefers other means of birth control, such as the coil, injections, vasectomies or, as a fallback, abortion? How do you ensure that condoms are sound in a country where quality control is everywhere elusive? How do you recruit health-workers to look after patients who are widely considered dangerous and undesirable? How do you get people to take HIV tests when they fear that a positive result will mean they lose their job, as infection with hepatitis often does already? How do you mend a broken public-health system?

But first of all China must find answers to the question of how to prevent a drugs-driven epidemic becoming a sex-driven one. If it does that, it has a good chance of containing AIDS. If not, it will discover that all its problems multiply, as Africa and, to a lesser extent, India have already found. China does not have much time.

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North Korea

A glimmer of hope?

Jul 28th 2005 | BEIJING
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Pyongyang lists its conditions for scrapping its nuclear programme

Get article background

AFP

Together again; how jolly!

AFTER shunning negotiations over its nuclear programme for more than a year, North Korea has finally begun talking again. But in return for scrapping its own projects, it is now asking the Americans for nuclear concessions. As a country that has declared itself a nuclear power, North Korea wants to be treated like one.

At the six-party talks including China, Japan, Russia and South Korea, which began in Beijing on July 26th, North Korea's delegate, Kim Kye-gwan, at least confirmed that his country's aim was the "denuclearisation" of the Korean peninsula. But he refused to accept America's version of what nuclear projects are under way in the North. America says they include the making of highly enriched uranium, which can be turned into nuclear weapons. North Korea admits only to a plutonium-based bomb-making project.

As the talks entered their third day, there was little obvious sign of progress beyond the fact that they were happening at all. Three earlier rounds, between August 2003 and June 2004, achieved nothing. In February this year, North Korea admitted publicly for the first time that it already had nuclear weapons and announced that it was withdrawing indefinitely from the negotiations. It was only after South Korea offered it a new and unconditional food-aid package and huge electricity supplies if it dismantled its weapons that it agreed last month to resume the talks.

But its effort to broaden the scope of the talks will complicate matters. According to South Korean officials, it wants America to withdraw its "nuclear umbrella" from the South. While the Americans are believed to have removed their nuclear weapons from South Korea itself in 1991, they still have missiles that could readily be used against the North.

Although America was not prepared to renegotiate its alliance with the South, a senior American official said he thought the parties could still forge a "common definition" of what was meant by denuclearisation. "If we have no intention to attack or invade [North Korea], doesn't that cover the issue of a nuclear umbrella?" he asked.

He also played down North Korea's refusal to admit to its uranium programme, a project the Americans claim the North acknowledged in 2002. He did not believe it would cause a problem "in terms of developing the principles" needed to frame an agreement, even though it still had to be addressed, he said.

Even if this was a hint that an agreement on dismantling North Korea's nuclear programme need not specifically mention uranium, the question will necessarily remain central to the implementation of any accord. The Americans say they do not know where any uranium-enrichment projects are located. This would make verification of their "non-existence" virtually impossible unless the North were ready to be more forthcoming.

The Americans say their offer to North Korea is much the same as the one made at the last round of talks in June 2004. Under it, North Korea was to be given three months in which to freeze its nuclear facilities, during which it would start receiving oil aid. Thereafter, it would be expected swiftly to dismantle the programmes under the supervision of inspectors. As this progressed, the Americans would

move toward lifting economic sanctions and removing North Korea from its list of terrorist states. But the North Koreans worry that this would require them to make concessions before they reap any rewards.

At least the format of the talks has been rather more flexible than in previous rounds. In the past, the Americans tried to avoid bilateral contacts with their North Korean counterparts. This time, the chief American negotiator, Christopher Hill (a newcomer to the process), has held three bilateral meetings with Mr Kim—much to the delight of the Chinese hosts. “The atmosphere has improved,” said a Chinese official. He may be clutching at straws.

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ASEAN

An alternative to Kyoto

Jul 28th 2005 | BANGKOK
From The Economist print edition

America unveils a new plan to combat global warming

Get article background

SUMMITS of the Association of South-East Asian Nations (ASEAN) are not known for suspense or surprises. But the regional club's latest pow-wow, which is due to conclude in Vientiane, Laos, on July 29th, involved plenty of both.

First, Myanmar's military regime waited until the last minute to announce that it would forgo ASEAN's rotating chairmanship, and so spare the group an embarrassing boycott. Then, at the ASEAN Regional Forum meeting, where South-East Asian countries get together with other Asian and Pacific nations, Australia agreed to sign a non-aggression treaty with the group in exchange for an invitation to yet another summit, where ASEAN hopes to start work on an East Asian free-trade area. But the biggest bolt from the blue was the announcement, by America and five Asia-Pacific countries, that they had devised a new pact to combat global warming.

The details of this non-binding “Asia Pacific Partnership on Clean Development and Climate” are fuzzy. But it emphasises technology transfers to reduce emissions of greenhouse gases, rather than the fixed targets and caps of the Kyoto protocol, the UN treaty on climate change. Rich countries might help poorer ones develop devices to cut carbon dioxide emissions from coal-fired power plants, for example.

Two of the signatories of the new pact, America and Australia, have already rejected the Kyoto agreement as too rigid. Two others, China and India, are not bound by the protocol as it applies only to developed nations. Indeed, of the six signatories to the new pact, only Japan and South Korea have formally ratified Kyoto. In theory, therefore, the “partnership” could enormously extend efforts to counter climate change. The countries concerned account for almost half the world's population, economic output and greenhouse emissions.

Environmentalists dismissed the deal as toothless. Many fear it will stymie efforts to persuade developing nations to sign up to Kyoto by the target date of 2012. The new pact's members insist that it will complement Kyoto, not supplant it. One Australian official claims that it is designed to reduce emissions faster than Kyoto would have. His country has devised a copper-bottomed plan to convince sceptics: another summit, to be held in Adelaide in November.

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Telecoms, television and the internet

The war of the wires

Jul 28th 2005 | SAN FRANCISCO
From The Economist print edition

Established telecoms companies are fighting an increasingly bitter battle against innovative attackers

"WE'RE not a telephone company anymore; I sort of resent that," says Lea Ann Champion, an executive at SBC, America's second-largest "Baby Bell". "We're a communications and entertainment company." Well, maybe. Ms Champion is in charge of "lightspeed", an SBC project to deliver TV, movies and other entertainment to customers via hugely enhanced broadband connections using internet protocol—a service known in short as IPTV. Lightspeed, which will cost $4 billion, has hit technological and legal snags recently that could slow its roll-out, scheduled to begin at the end of this year. But sooner or later IPTV will happen, if only because telecoms companies all over the world are betting on it. And when it does it will be controversial.

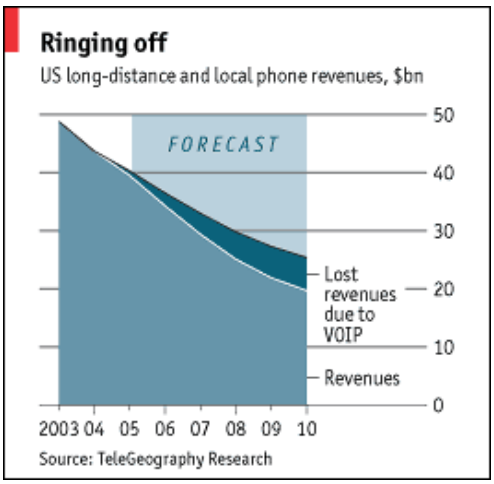
That is because IPTV forms part of a larger, and quite desperate, defensive strategy now being adopted by telecoms firms against fierce attacks on multiple fronts. On one front are cable giants, such as America's Comcast, which are luring customers with an enticing "triple-play bundle" of TV, broadband and telephony services. On a second front are mobile-phone operators, which young customers in particular are increasingly using to "cut the cord" from their fixed-line company.

But arguably most dangerous of all is the third front, where traditional telecoms firms are under attack from voice-over-internet-protocol (VOIP) providers, which use the internet to carry conversations that would previously have taken place via a conventional phone. TeleGeography, a research firm, estimates that the number of subscribers to VOIP services such as Vonage, which lets users plug their traditional phones into a gadget connected to the internet, will grow from 1.8m at the start of this year to 4m by the end of December in America alone; by 2010, it projects over 17m American subscribers. This does not count the world's largest VOIP provider, Skype, which uses a small and simple software application to let users make free calls between computers—so far, it has been downloaded 141m times.

Hanging on the telephone

Traditional telecoms firms are doing their best to respond to these threats by adopting internet technologies themselves. This week, VSNL, the top operator in India for international calls, said it would buy Teleglobe, the world's largest international wholesale VOIP carrier. Every big telecoms firm is investing to migrate from old, circuit-switched networks to new internet-based ones, with Britain's BT probably moving fastest. The threat from VOIP would then be neutralised, as the telecoms firms

themselves would be providing it. Even so, VOIP makes already grim revenue forecasts for old-style telecoms firms look truly depressing (see chart).



Hence IPTV—a sort of last-ditch charge by a cornered beast. For by switching to fast, new internet-based networks, telecoms companies will also be able to catch up with their cable rivals by offering entertainment, internet access and voice services over their networks. Better yet, those telecoms firms that also own mobile-phone subsidiaries might outdo their cable rivals by adding cellular service, to create a “quadruple-play bundle”.

Yet IPTV is an extremely risky strategy. To deliver it, the telecoms firms must first provide huge bandwidth to their customers. Some, such as BT, are doing this by souping up their existing copper lines into homes, which is costly, while others, such as America's Verizon and SBC, are also laying new fibre in the ground, which is outrageously costly. The firms will then put a box, called a “residential gateway”, into customers' garages or basements, which will connect at blazing speeds to computers and telephones as well as to a set-top box by the TV. Family members can then make phone calls, surf the web, and watch movies simultaneously, all via one “pipe”.

Technological glitches are possible. The bandwidth may prove insufficient, or the digital-rights and compression formats could prove too fiddly. But the industry is playing down such risks. “The issues are not technical but regulatory and cultural,” says Tim Krause, a manager at Alcatel, a firm that supplies the necessary infrastructure to IPTV operators such as SBC.

The main cultural risk, says Albert Lin of American Technology Research, a consultancy, is that telecoms firms, which have not hitherto been seated at the best tables in Hollywood restaurants, will not be able to buy rights to films and shows that anybody actually wants to watch. This suggestion infuriates the telecoms firms. The doubters “are just plain wrong,” says Michael Coe, a spokesman for SBC. “There are no barriers to acquiring content. The only question is: what will it cost?”

Having literally sunk their billion-dollar investments in the ground, the telecoms firms will need to get a decent return on them. But in their nightmare scenario, customers may simply sign up to their huge bandwidth and then use it not to buy the services touted by the telecoms firms but instead to obtain independent or web-based services, such as Skype for making calls or (when the service is launched) Netflix for downloading movies. Can the telecoms firms do anything to stop that?

Stoyan Kenderov, an IPTV expert at Amdocs, a firm that makes back-office software for telecoms companies, says that the telecoms firms are building into their residential gateways new technology that will inspect the packets of zeros and ones passing through. This will let them identify traffic from third-party rivals, which might then end up at the back of the queue and thus be slow and patchy. The only hint that users might have of that going on, says Mr Kenderov, would be some very fine print on their bills explaining, in turgid legalese, that the provider guarantees the quality of its own services only.

The telecoms firms counter such suggestions with well-rehearsed indignation. In a hearing before the judiciary committee of America's Senate in March, Edward Whitacre, SBC's chairman, said in emphatic Texan that “SBC would not block any Vonage traffic or anybody else's and has never done that, would not do that. That's not the way we do business, and it's just not going to happen.”

Cyrus Mewawalla of Westhall Capital, a brokerage, predicts that “at some point the world VOIP market will experience a massive security scare,” when viruses or other banes of the internet make themselves felt in the world of the new services. At that point, Mr Mewawalla says, customers will “flock in droves back to the big boys who own their own networks”, such as SBC or BT, and “desert those who use the public internet”, like Skype or Vonage.

The packet-monitoring technology that the telecoms firms are installing can be used—legitimately—to enhance security and quality. It can also be used—though it will be hard to prove—to degrade the services of rivals. The only true protection against that outcome is more competition between broadband access providers (cable and telecoms firms; new technologies such as WiMax, a wireless system that, one day, may cover entire cities, and broadband over power lines). But given the tactics of the incumbent telecoms firms, it may fall to regulators to ensure that this essential competition develops.

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Music scandals

Sing a song of Spitzer

Jul 28th 2005
From The Economist print edition

Sony BMG admits to bribing radio stations to play its artists

Get article background

IN 1980, according to a book about the music industry by Fredric Dannen called “Hit Men”, CBS Records decided to run an experiment with a band, Pink Floyd. Their concert dates were sold out in Los Angeles, and radio stations everywhere were playing “Another Brick in the Wall (Part Two)”. Dick Asher, the deputy president of CBS Records, wanted to find out whether the band's popularity meant he could refuse to pay the usual bribes, or illegal “payola”, to the four big Top-40 radio stations in Los Angeles. Like stations across the country, they claimed to make independent choices based on taste. But Mr Asher lost; only after Pink Floyd's manager insisted that CBS Records hand over the money did the stations spin the record.

Payola began in the 1950s and it is still rampant today. This week Sony BMG, a leading record label, apologised and agreed to pay a fine of $10m for bribing radio stations. New York's hyperactive attorney-general, Eliot Spitzer, said that bribes are pervasive in the industry, and that he is continuing his investigation into the other big record labels—Universal, EMI and Warner Music—as well as the radio business.

That seems fair: the radio industry, after all, is just as much to blame for payola. Employees at Clear Channel, America's biggest radio company, crop up frequently in the incriminating e-mails that Mr Spitzer published this week. The bribes they received came in the form of electronic goods, free airline tickets and hotels, sneakers and musical instruments and equipment. Some of the methods its labels used were quite basic, such as hiring girls to call in posing as listeners with requests for songs.

Radio play is by far the most effective way to promote a new artist and to sell records. There is massive competition for the slots on a popular radio show, so the temptation to bribe is enormous. Small music labels often suffer because they cannot afford it. Nor do the big labels like the system, though they have made use of it. In 2002 a coalition of artists, other groups and the Recording Industry Association of America, which represents the labels, wrote to the Federal Communications Commission asking for an investigation of payola.

Although the overall impact of payola is negative, it has sometimes helped great music reach an audience. Radio companies choose music centrally, test it on focus groups, and tend to reject any that does not fit the mould. The Sony BMG documents show that payola was used to get a song by Jennifer Lopez on the air. Yet a band called Audioslave, which makes more “challenging” music, also benefited. “I've paid payola,” admits one music executive. “I couldn't get through to the key radio stations, my band made difficult music and now they're a household name.”

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European telecoms

Spanish step

Jul 28th 2005 | PARIS
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France Télécom enters Spain's mobile-telecoms market

FRANCE TELECOM caused a stir in European telecom circles on July 27th when it bought an 80% stake in Amena, Spain's third-largest mobile-phone operator. At a recent presentation of his strategy for the next three years Didier Lombard, boss of the hugely indebted French telecoms group, seemed to rule out big acquisitions this year. And France Télécom had been a late, final bidder in the auction for Amena, which had started in April.

Auna, the parent of Amena, had until recently been up for sale in its entirety. Several consortia, including private-equity firms, had been interested in acquiring the group, which also provides cable-TV and internet services. But France Télécom wanted only Amena—and when Auna belatedly decided to sell it separately, it tabled a bid that valued the firm at €10.6 billion ($12.7 billion)—more than ten times its operating profit last year—exceeding the second-highest bid by around €600m.

Is France Télécom paying too much? It is still suffering from squandering a fortune on buying Orange, another mobile-phone company, in 2000. That deal cost France Télécom an absurd €40 billion. Yet this time is different, it claims. It is justified in paying more than its various rivals for Amena because it will benefit from a €1.7 billion tax credit for goodwill amortisation that will only be granted to a Spanish purchaser (it is using its Spanish subsidiary to make the acquisition). It also expects to save €1.1 billion by exploiting synergies.

Adding Amena to Uni2, its fixed-line operator in Spain, and Wanadoo, its internet service, will allow France Télécom to offer the same all-inclusive package as it does in France, Britain, Poland, the Netherlands and Belgium. The deal has a strong strategic rationale, say analysts at Exane BNP Paribas, a brokerage.

Currently, three big companies—Telefónica, Britain's Vodafone and Amena—dominate the Spanish mobile-phone market, which is now growing strongly. However, France Télécom concedes that a price war is possible—especially if “virtual” mobile-network operators (who buy access to operators' networks and resell mobile-phone service under their own brands) enter the Spanish market, as they have in other countries. So far they have not done so, not least because the big network operators have been uncooperative. But several would-be virtual operators are lobbying the regulator to force the networks to give them a better deal.

The purchase of Amena may prove to be a crucial step in the consolidation of European telecoms. So far this year KPN and Telfort have merged in the Netherlands, Ireland's Eircom has bought Meteor, a mobile operator, Wind, an Italian mobile operator, has been acquired by an Egyptian consortium with ties to Orascom and, last year, Denmark's TDC bought Sweden's Song. “France Télécom's takeover of Amena could herald the return of large strategic deals in European telecoms,” says Paulo Pereira, head of European mergers and acquisitions at Morgan Stanley, an investment bank.

For France Télécom, this may be the last big deal in Europe. It now wants to focus on countries where it can offer its integrated model, which rules out Germany, Italy and Austria. And Mr Didier promises to tread carefully outside Europe, as he thinks another telecoms bubble is forming. For instance, in June, Spain's Telefónica offered far more than any rival bidder for Cesky Telecom, a Czech telecoms operator. Of course, so too did France Télécom for Amena—but the French insist that, in their case, this was due to good business logic, not irrational exuberance.

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The media in India

Popping corks

Jul 28th 2005 | DELHI AND MUMBAI
From The Economist print edition

Far more news than is fit to print?

TO THE envious eyes of the Western journalist, veteran of the gruelling advertising recession of this century's early years, it is a glimpse of a legendary golden age. In the brasserie of one of Mumbai's swankiest hotels, a newspaper editor and a dozen of his senior staff are sipping champagne at three in the afternoon. At the end of an expensive lunch, they are preparing for a launch, a few weeks off.

This week, as Mumbai ground to a halt under the worst monsoon deluge anyone can remember, life could not have been grimmer for everybody. But it is still a good time to be an Indian journalist. July 30th was due to see the birth of *DNA—Daily News & Analysis*—the third English-language paper launched in Mumbai so far this year. Add the prospect, nationwide, of no fewer than six new cable-television news channels by the end of the year, and jobs are multiplying and salaries soaring.

Competition between the new papers has been fierce already, for market share as well as for staff. For months Mumbai's hoardings have been advertising *DNA*'s arrival, with posters showing random citizens voicing their opinions (eg, “I wish I could educate the education system”, or “Do I really want to know who is wearing what at Cannes?”) and the exhortation: “Speak up. It's in your *DNA*.”

The *Times of India*, with a circulation in Mumbai of 600,000 and half of the city's English-language market, responded with a copycat campaign (withdrawn when *DNA* sued) and, in May, the launch of a new tabloid, the *Mumbai Mirror*. Then, earlier this month, the *Hindustan Times*, a Delhi-based broadsheet, launched a new Mumbai edition.

Several trends are coming together in Mumbai's newspaper wars: a breakdown in the regional carve-up of India that many papers used to observe; a strong economy, which this week saw the stockmarket scale new heights; and a healthy appetite among investors for fresh news outlets.

Until a few years ago, most of the big English papers had an understanding to stay off each other's turf: the *Times* in Mumbai, *Hindustan Times* in Delhi, *Telegraph* in Kolkata (Calcutta) and the *Hindu* in Chennai (Madras). It was the *Times* that broke up this cosy consensus with a circulation drive in Delhi, where it and the *Hindustan Times* now compete fiercely for leadership in a market of more than 2m.

Mumbai has a larger population than Delhi and, says Girish Agarwal of *DNA*, more English-language readers. Yet the market for English papers there is only half the size. That, he says, is what makes Mumbai attractive for *DNA*'s owners—a joint venture of Zee, a TV station, and Dainik Bhaskar, which produces one of the biggest-selling Hindi-language papers. Mumbai is also the origin of a big chunk of India's total advertising spending.

But the enthusiasm of investors both at home and abroad for India's news media spreads beyond Mumbai and English—the language, says Farokh Balsara of Ernst & Young, of only three of the 50 top-selling papers. This week, the *Hindustan Times* announced plans to raise up to 3.7 billion rupees ($85m) in a stockmarket listing. In May, Independent News & Media, an Irish publisher, bought 26% of Jagran Prakashan, publisher of the biggest-circulation daily. Last year, the *Financial Times*, half-owner of *The Economist*, acquired 14% of the *Business Standard*, an English-language daily.

The action is yet more frenetic in cable-TV news although, as with papers, foreigners are limited to a 26% stake in TV firms. Some 44m homes will soon have access to their cable operator's choice from 32 news channels, about ten of them in English. The planned new arrivals include one produced by Bennett, Coleman (owners of the *Times*) and Reuters; a new “global news” offering from Zee; one fronted by Rajdeep Sardesai, a well-known television reporter; and a fourth channel from NDTV, the station that Mr Sardesai quit.

India is a good place for journalists not just because new outlets for their work are proliferating, but also because the country is a mine of great news stories. Yet the news wars will not be free of casualties. Better crack open another bottle now, before it is too late.

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The car industry

Malaysia's motor mess

Jul 28th 2005 | KUALA LUMPUR
From The Economist print edition

Who can solve Proton's problems?

AP

Shame about the supply-chain glitches

IS PROTON, Malaysia's molly-coddled state-controlled carmaker, finally set for a shake-up? On July 25th, the firm fired its chief executive, Tengku Mahaleel Ariff. His immediate offence was to criticise the government for allowing too many imported cars into Malaysia, thereby, he claimed, denting Proton's profits. But he had also resisted the idea that the government should sell a large part of its stake in Proton to a foreign carmaker. Proton's minority of publicly-traded shares jumped by over 8% on the day after his dismissal, presumably on hopes that a big sale will now go ahead.

Proton should be king of Malaysia's roads, thanks to the steep tariffs and excise duties imposed on imported cars and even locally-assembled foreign brands. But despite such protection its market share has slipped steadily, from 66% in 1999 to 40% in the first six months of this year. The firm sold less than 190,000 cars last year, far below its capacity of 380,000. Profits, needless to say, are as lacklustre as sales.

The government has pledged to reverse this slide many times. At one stage, Proton pinned its hopes on exports. But last year, it sold only 17,000 cars overseas. The launch of a new model—Gen.2—was also supposed to revive the company's fortunes, but poor design and supply-chain glitches put paid to that. The root of the problem is Proton's modest size, says Edward Ong, an analyst at Macquarie, a bank. It cannot hope to achieve the same economies of scale as competitors such as Toyota, Kia and Hyundai, each of which churned out millions of vehicles last year.

One solution would be to sell Proton to a big foreign firm. Chinese companies may be interested, but Volkswagen is the obvious candidate, having signed a deal last October promising to help Proton to develop new models in exchange for the use of Proton's plants to make its own cars. Such a sale would fit in with the government's recent drive to revamp management and increase efficiency in Malaysia's state-owned firms. The chairman of Proton's board has even suggested that the next chief executive might be a foreigner.

But Mahathir Mohamad, a former prime minister who helped to create Proton and now acts as an adviser, says he is opposed to foreign ownership on principle. He is already kicking up a stink about Mr Mahaleel's dismissal. Such nationalistic tirades go down well with Malaysia's ruling party, the United Malays National Organisation. Indeed, many UMNO members and government officials believe that state-owned firms such as Proton should put national development and the welfare of ethnic Malays above a grubby fixation with the bottom line.

Abdullah Badawi, Dr Mahathir's successor as prime minister, faces a further dilemma. Malaysian consumers would definitely benefit from stiffer competition, and that would probably be the best medicine for Proton too, in the long run. But Khazanah, the government's holding company, will have difficulty selling a big stake in Proton to a foreign firm unless the authorities promise to maintain its privileges for a while. No wonder the government keeps putting off its announcement of a new national automotive policy.

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Pharmaceuticals

Big generic pharma

Jul 28th 2005 | JERUSALEM AND NEW YORK
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A merger creates a global generics giant

RUMOURS that Teva, Israel's largest pharmaceutical firm and worth one-fifth of the Tel Aviv stockmarket, was on another buying spree had circulated for weeks. Many thought it would snap up one of the Indian firms that, like Teva, specialise in making generic drugs—copies of branded drugs that usually sell for a fraction of their price. Instead it went for Ivax, an American firm that in the 1980s was Teva's rival in size but will now—after this week's $7.4 billion deal—make Teva once again the biggest generics firm in the world. Teva had slipped briefly to number two when Novartis of Switzerland agreed in February to buy Hexal, a German generics company, and Hexal's American partner, Eon Labs, merging them into Sandoz, Novartis's generics division.

The generics industry in America has been booming in the past five years as patent protection has expired on one famous blockbuster drug after another, making them fair game for generics manufacturers to copy. This year, generic drugs will account for more than half of all the drugs prescribed in America by volume, up from one-third in 1990.

Research and development for a generic drug costs only a couple of million dollars instead of hundreds of millions for a genuinely new drug, so it can be an easy business to enter. However, much of the important action takes place in court—where branded drug makers try to prolong their patents by tweaking their drugs, while generic firms try to break patents early to grab market share before rivals.

Firms in some countries, such as India, have been able to copy drugs much earlier than those in America and Europe because of weak patent protection. Teva, which began in 1901 as a wholesaler and importer of drugs, at first grew in part because Israel's lack of data-exclusivity laws allowed it to learn the formulas of imported drugs from the government, after their manufacturers filed the data to get regulatory approval. Israel passed a data-exclusivity law this year, but that was not good enough for the American government, which added Israel to its “Priority Watch List” of 15 countries whose intellectual-property protection it considers substandard.

Teva has also been busy in the takeover market, accumulating by far the world's longest list of generic drugs pending approval. It has a good record of integrating other firms into its business. Ivax should boost its sales in Latin America and central and eastern Europe—now, nearly two-thirds of its sales are to North America.

Teva has also been carefully diversifying, including into developing proprietary drugs, such as its profitable new treatment for multiple sclerosis. Last year it bought Sicor, a biotech firm that will help it in the nascent market for “biogenerics”, which is expected to mushroom in the next few years as American and other national regulators yield to the growing pressure to cut the cost of biotech drugs by licensing the first generic versions of them.

Although it is the biggest generics firm, its worldwide market is highly competitive. Teva's sales account for only 12% of it. And new competitors are entering, among them big pharmaceutical firms, led by Novartis, that are themselves trying to diversify into generics. As countries with weak intellectual-property laws tighten them up (India did this year), their generics firms will join the world market, too. Generics companies will need solid foundations to survive. For now, though, none are more solid than Teva's.

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Farm monopolists

Jurassic twilight

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Canada's and Australia's wheat-export monopolists risk extinction

DINOSAURS live. Two have been roaming the Canadian prairies and parts of Australia, respectively, for decades, and are still at it: the two countries' legally enforced wheat-export monopolies. But till when? American farmers think it is time they were extinct. They came under fire at this month's World Trade Organisation talks in China, and if its new trade round is to live, the two most probably must die.

American farmers have no objection to rigged markets. They love their own subsidies and protection. But recent weeks brought them bad news on both. George Bush spoke openly of cutting American farm subsidies if the European Union (EU) would do so too. It was no secret that both must cut, if the WTO round is to succeed, but this still shocked the prairies. And an American wheat tariff that has hit imports from Canada since 2003 was denounced by a North American Free Trade Agreement (NAFTA) panel. After that double whammy, both foreign wheat monopolies were obvious targets for retaliation.

The two bodies, between them controlling about one-third of the world's annual 100m-plus-tonnes of wheat exports, are certainly oddities in these days of free trade. In 1935, Canada's wheat-growers were going bust. So a state-run but voluntary body was set up to market their crops collectively and get better prices. In wartime 1943 it became compulsory. Today, the Canadian Wheat Board (CWB) is still compulsory, still state-controlled, and still has a monopoly of all west-Canadian wheat (and barley) exports. In some years, it is the biggest grain-exporting body in the world. And America is fed up with it.

In 2003, after repeatedly attacking CWB's monopoly and alleged state subsidies, the Americans, seeing it take 20-25% of their own demand for hard red spring wheat and durum (pasta wheat), slapped on duties of 4%, later raised to 14%. That killed the trade. Meanwhile the Americans had also denounced the CWB to the WTO.

They got a surprising answer: like it or not, the CWB's monopoly did not break WTO rules. Canada hit back, calling first for a WTO probe of the American duties, then backing off to one by NAFTA. But last July the WTO called for new restraints on all farm monopolies such as the CWB. The EU too is hostile: it made plain in China that if it is to cut export subsidies, others must end export monopolies.

Less predictably, some west-Canadian farmers are hostile, too. Why should they be forced to sell their grain for export—and inside Canada, if for human use—to a single agency, on its terms, at its “pool” price? The CWB is still state-run, which also rankles, although growers now elect ten of its 15 directors. It claims that it gets a premium price, but critics say they could do better themselves. If others want to sell through it, fine—but let all be free to choose.

Australia's “wheat board” is odder still. Officially, it no longer exists. Set up in 1939, it was privatised in 1999 and, as plain AWB, is now quoted on the stockmarket. Yet it still has a legal monopoly of all but the smallest exports. And, just by the way, in 2003 it bought Australia's largest supplier of farm inputs and handler of 20% of the wool clip and livestock trade.

It faces little criticism from Australia's 40,000 wheat growers. They want more information on AWB's supply-chain costs, so they can judge alternatives better. But they firmly support its bulk-export monopoly, reckoning its pool prices earn them more than they would get from the world's mighty commercial traders.

They may be right. As AWB proclaims, it ensures “that Australian growers are not played off against each other” and that “the price for Australian wheat cannot be bargained down”. To “Australian” add “Canadian” and that, say their critics, is precisely what's wrong with AWB and the CWB: they do what monopolies are meant to—they enrich sellers, at buyers' expense.

But by how much? In the world market, they are but two among many sellers. They are no more monopolists, argue supporters, than Toyota is in a car market with plenty of rivals. The real free-market case against them may be the opposite: their power inside the two countries, especially Canada, as dominant buyers.

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Product placement

On Broadway

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How to hedge a toe-tapping, finger-snapping, big-budget gamble

PUTTING on a Broadway show is one of the bigger gambles in America's entertainment industry, with investments running into the millions of dollars with little assurance of a return. It can take at least two years for a successful show to pay back its original investment, and only one out of five shows manages even that, according to the League of American Theatres and Producers.

Given the dicey economics of the New York stage, especially for musicals (which can cost around $10m to put on), it seems understandable that producers are becoming more creative in how they raise funds. This creativity resulted in a fairly controversial move in May, when a Broadway revival of Neil Simon's "Sweet Charity" tweaked a line of dialogue that had referred to whiskey: "Grand Centenario, the tequila?", a waiter now asks. Mr Simon himself agreed to this change, which mentions a sponsor, and the tequila's logo decorates the set. This bold move came not long after Yahoo! and Hormel Foods, maker of Spam, sponsored the triumphant Monty Python musical, "Spamalot", and Turtle Wax endorsed (but was unable to save) the ill-conceived "Good Vibrations".

While sly marketing strategies have long inhabited film and television—to the dismay of Jonathan Adelstein, a commissioner at the Federal Communications Commission, who has called for a probe of more covert pitches—many have taken an "is nothing sacred?" attitude to the brandishing of brands on stage.

Marketing companies claim to be exercising (relative) restraint—though for how much longer? "We are extremely careful not to go out of our way to take a product and squeeze it into the show," says Tanya Grubich of the Marketing Group, which manages marketing campaigns for such Broadway shows as "Wicked", "Avenue Q", and "The Producers". Instead, they claim, they search scripts for items that can be sponsored, typically through a donation, and contact businesses to arrange partnerships and product tie-ins. (Cash deals are rarer than barter arrangements, although some have netted a production as much as $1m.) Baz Luhrmann's "La Bohème" involved a deal with Montblanc, a maker of fine pens, to feature an antique company sign on stage in exchange for window displays and a special pen in Montblanc stores. Alas, the 2003 show still lost around $6m.

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Face value

A Wal-Mart for the granola crowd

Jul 28th 2005
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John Mackey sees no limit to the appetite for natural foods

NO ONE admits to being more surprised by the runaway success of Whole Foods Market than its boss. "In all my profound wisdom I decreed a maximum of 100 stores, and thought that would saturate the United States," recalls John Mackey of the time when his company went public in 1992. That in itself was quite a milestone for a grocery retailer that he began in 1978 in a garage in Austin, Texas, when he was living in a vegetarian co-op. At first, hippies and college students were his main customers. But now, with over 170 stores feeding America's organic-food-addicted middle class, Whole Foods Market has become firmly established as the world's largest natural-foods chain.

Nor is there any sign of the firm's rapid growth coming to an end. Its sales rose by 23% to $3.9 billion in the latest financial year. Mr Mackey is now expanding the firm abroad, initially with a move to London. As for the success of this, a chastened Mr Mackey says, "we actually don't have the least bit of doubt".

To understand the allure of Whole Foods Market, look no further than the new landmark store that it opened in Austin, Texas earlier this year. Occupying almost 80,000 square feet (7,300 square metres), it is one of the firm's largest, and features a vast array of treats, from organic enchiladas to an in-house meat smoker. There are sampling stations, cooking demonstrations and café tables galore. Employees, called "team members", are as enthusiastic as the shoppers, and gladly explain company policy on, say, sustainable fishing (no Chilean sea bass, for instance, as it is seriously overfished). The firm is starting to label its own-brand foods to indicate any genetically modified ingredients.

Yet fancy food is just one part of the recipe. Whole Foods Market is also deeply committed to its "green mission". "We see the environment as a stakeholder in the business," says Mr Mackey who, no surprise, lives his brand. Trim and fit, he prowls the office in shorts and a handyman-style canvas shirt, and is very much the outdoors type. This summer he is hiking along part of the Pacific Crest Trail, which runs from Mexico to Canada.

The firm's environmentalism is decentralised: each store is encouraged to experiment, and implement what best suits its own circumstances. So, for example, the California stores use solar power, taking advantage of subsidies provided by the state government. In other locations, some use wind energy. Newer stores, such as one in Sarasota, Florida, are pioneering new types of "green building", for instance, using recycled materials. Successes and failures are shared via the internet.

Yet Mr Mackey's organic idealism and greenery should not be confused with a lack of hard-nosed business acumen. He can quote Adam Smith with the best of them. He is often criticised for wiping out the small, local natural-food businesses that, not so long ago, were what the industry was all about. He is also opposed to trade unions. Whole Foods Market workers in Madison, Wisconsin, caused a stir three years ago when they voted to join a union, but the company persuaded them to back down. Currently his stores remain non-union. Mr Mackey says he dislikes the “adversarial nature” of labour unions—the “zero-sum mentality” whereby “if shareholders are winning, labour is losing”. The market, he says, is the “best check against exploitation, because people can vote with their feet.” Indeed, says Roy Bingham of Health Business Partners, an investment bank, Whole Foods Market benefits from the undying keenness to work for it of the “sandals brigade” of young idealists. The firm is regularly cited by *Fortune* as one of the top 100 places to work in America.

If there is something familiar about a giant, anti-union retailer crowding out small local businesses, Mr Mackey rejects any comparison with Wal-Mart—well aware of the battering that the world's biggest retailer has taken because of its relentless growth. “It's like comparing a Hyundai car to a Lexus,” he says. “Wal-Mart's focus is on getting the cheapest stuff in; we're focused on getting the best stuff.” That said, Wal-Mart is starting to offer organic and natural foods as it pursues wealthier customers. This may spell trouble some day for Whole Foods Market. For all its growth, the company is still dwarfed by Wal-Mart, which had revenues last year of $285 billion.

Also unusually for the organic-food industry, but in common with Wal-Mart, Whole Foods Market has grown partly by acquisition, buying chains such as Fresh Fields, Bread & Circus and, in London, Fresh & Wild. More acquisitions may follow abroad. Although there is now little left to buy in America, Mr Mackey still sees opportunity to grow there. Whole Foods Market currently has a presence in only 39 of the country's top 50 metropolitan markets. “None of those markets has reached saturation, plus the whole market is continuing to rapidly expand,” he says. As for Europe, Mr Mackey wants to open a big Whole Foods Market store in London, but has yet to find the right site. If London does well, then he would move aggressively into continental Europe.

Now in your basement

Always looking for new opportunities, Mr Mackey is now trying to combine organic food with the other craze gripping America's middle class: real estate. The idea is to build Whole Food Market stores into apartment-building basements. “In urban areas like New York or London, land is so expensive that it really helps to make our stores more affordable if we can get multi-use developments on top of us,” says Mr Mackey. “And housing is perfect because it doesn't compete with us and in fact gives us customers” who enjoy direct access by elevator to the store.

So, is there anything that could cause Whole Foods Market to choke? “You know, I'm not a worrier,” says Mr Mackey. Barring some freak event such as food terrorism, Whole Foods Market seems set for more success. Mr Mackey certainly seems relaxed about the future. When trekking through the wilderness, he does not even bother to carry a mobile phone.

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China and the world economy

From T-shirts to T-bonds

Jul 28th 2005
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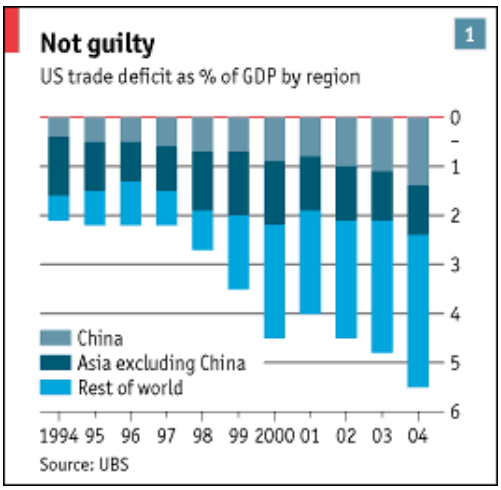
Beijing, not Washington, increasingly takes the decisions that affect workers, companies, financial markets and economies everywhere

Get article background

GLOBAL tremors in the currency, bond and commodity markets greeted China's announcement that the yuan will no longer be pegged to the dollar. No longer is it just Washington that has the power to cause shockwaves. For many people, the tremors reflected the view that China is the root cause of America's trade deficit, and that the revaluation is a partial cure.

In fact, that view is wrong on several counts. China is not the main cause of the American trade deficit. On the other hand, China is behind almost everything else going on in the world economy. For China is beginning to drive, in a new and pervasive way, economic trends that many countries assume to be domestically determined.

Americans like to slap the “made in China” label on their huge trade deficit. Yet not only is China's forecast current-account surplus of around $100 billion this year only a fraction of America's likely deficit of $800 billion, but, as chart 1 shows, most of the increase in America's trade deficit has come from outside China. The main cause of America's trade deficit is a lack of domestic saving, not unfair Chinese competition. The deficit is thus made in America, not made in China.



As for last week's revaluation, the announcement marked a significant break with the past. China has long been under pressure to revalue its currency from countries that claim the undervalued yuan gives Chinese exporters an unfair advantage. After pegging the yuan to the dollar for a decade, China has shifted to a managed float against a basket of currencies, with an initial revaluation against the dollar of 2.1%. Nobody is yet sure how this will work. It may be just a token move aimed at warding off American protectionism. Or it could be the first of several revaluations, marking the end of the so-called “revived Bretton Woods system”, under which China and other Asian countries have bought billions of dollars in foreign-exchange reserves to hold their currencies steady against the greenback.

Either way, the tiny revaluation by itself will have little impact on America's huge trade deficit. Indeed, even if the yuan is allowed to rise by another 5-10% over the next 12 months, as many economists expect, that would hardly make a dent in the deficit. Nevertheless, it is still an important change in China's exchange-rate regime, representing a step towards a market-based system. And, as

such, it could have implications for the dollar, bond yields, and American consumer spending.

To view China's global impact mainly in terms of its exports and its trade surplus is to misunderstand, and to underestimate, the profound forces behind China's growing influence. Everyone knows that most TVs and T-shirts are made in China. But so, in some ways, are developed countries' inflation rates, interest rates, wages, profits, oil prices and even house prices—or at least they are strongly influenced by what happens in China.

Of course, China is not the only fast-growing emerging economy that is making waves around the world. But China really does loom much larger: its contribution to global GDP growth since 2000 has been almost twice as large as that of the next three biggest emerging economies, India, Brazil and Russia, combined. Moreover, there is another crucial reason why China's integration into the world economy is today having a bigger global impact than other emerging economies, or than Japan did during its period of rapid growth from the mid-1950s onwards. Uniquely, China combines a vast supply of cheap labour with an economy that is (for its size) unusually open to the rest of the world, in terms of trade and foreign direct investment. The sum of its total exports and imports of goods and services amounts to around 75% of China's GDP; in Japan, India and Brazil the figure is 25-30% (see chart 2). As a result, the dragon's awakening is more traumatic for the rest of the world.

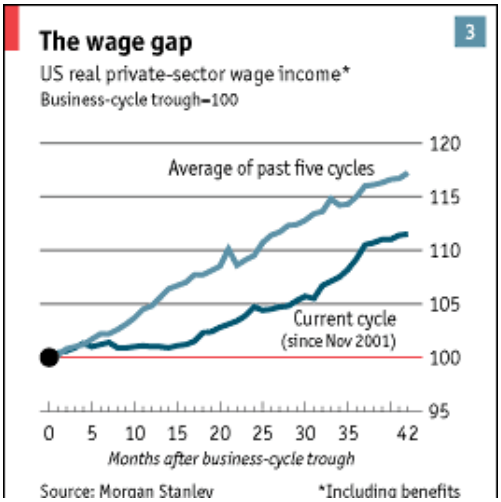
Doubling the world's workforce

Most analysis of China's growing importance focuses on its rising share of global output and exports. That, in turn, fuels fears that China is stealing production and jobs from the rest of the world. But this misses half the story. It is true that China's trade surplus has increased sharply this year—mainly because the government's efforts to cool fixed investment have cut back imports. But over the past decade, China's imports have risen at the same pace as its exports. So China is giving a big boost to both global supply and demand.

China's impact on the world economy can best be understood as what economists call a “positive supply-side shock”. Richard Freeman, an economist at Harvard University, reckons that the entry into the world economy of China, India and the former Soviet Union has, in effect, doubled the global labour force (China accounts for more than half of this increase). This has increased the world's potential growth rate, helped to hold down inflation and triggered changes in the relative prices of labour, capital, goods and assets.

The new entrants to the global economy brought with them little capital of economic value. So, with twice as many workers and little change in the size of the global capital stock, the ratio of global capital to labour has fallen by almost half in a matter of years: probably the biggest such shift in history. And, since this ratio determines the relative returns to labour and capital, it goes a long way to explain recent trends in wages and profits.

In America, Europe and Japan, the pace of growth in real wages has been unusually weak in recent years. Indeed, measured by the growth in income from employment, this is America's weakest recovery for decades. According to Stephen Roach, an economist at Morgan Stanley, American private-sector workers' total compensation (wages plus benefits) has risen by only 11% in real terms since November 2001, the trough of the recession, compared with an average gain of 17% over the equivalent period of the five previous recoveries (see chart 3). In most developed countries, average real wages have lagged well behind productivity gains.



The entry of China's vast army of cheap workers into the international system of production and trade has reduced the bargaining power of workers in developed economies. Although the absolute number of jobs outsourced from developed

countries to China remains small, the threat that firms could produce offshore helps to keep a lid on wages. In most developed countries, wages as a proportion of total national income are currently close to their lowest level for decades.

The flip side is that profits are grabbing a bigger slice of the cake (see chart 4). Last year, America's after-tax profits rose to their highest as a proportion of GDP for 75 years; the shares of profit in the euro area and Japan are also close to their highest for at least 25 years. This is exactly what economic theory would predict. China's emergence into the world economy has made labour relatively abundant and capital relatively scarce, and so the relative return to capital has risen. It is ironic that western capitalists can thank the world's biggest communist country for their good fortune.

China's main impact on the world economy is to change relative prices and incomes. Not only are the prices of the goods that China exports falling; the prices of the goods that it imports are rising, notably oil and other raw materials. China is already the world's biggest consumer of many commodities, such as aluminium, steel, copper and coal, and the second-biggest consumer of oil, so changes in Chinese demand have a big impact on world prices.

China has accounted for one-third of the increase in global oil demand since 2000 and so must bear some of the blame for higher oil prices. Likewise, if China's economy stumbles, then so will oil prices. However, with China's oil consumption per person still only one-fifteenth of that in America, it is inevitable that China's energy demands will grow over the years in step with its income.

There is currently only one car for every 70 people in China, against one car for every two Americans. That implies a huge increase in oil demand, which could keep prices high for the foreseeable future, because of scarce global spare capacity. China's consumption per person of raw materials, such as copper and aluminium, is also still low, so rising demand will continue to support commodity prices.

Cheap money

Overall, the upward pressure that Chinese imports of raw materials have put on the prices of oil and other commodities has been more than offset by the downward pressure of Chinese manufactured exports. As a result, another important aspect of the China effect is low inflation.

Central bankers like to take all the credit for the defeat of inflation, but China has given them a big helping hand in recent years. China's ability to produce more cheaply has pushed down the prices of many goods worldwide, as well as restraining wage pressures in developed economies. For instance, the average prices of shoes and clothing in America have fallen by 10% over the past ten years—a drop of 35% in real terms.

A study by Dresdner Kleinwort Wasserstein reckons that China has knocked almost a full percentage-point off America's inflation rate in recent years. The recent 2% revaluation of the yuan will probably be absorbed by Chinese manufacturers trimming their profit margins and so will not be passed on into export prices. But Americans calling for a 25-30% revaluation may come to regret it: the result would almost certainly be faster inflation.

As it is, China's reduction of inflationary pressures has allowed central banks to hold interest rates lower than they otherwise would be. Three and a half years into its recovery, America's real short-term interest rates are only 0.7%, almost two percentage-points below their average at the equivalent stage in previous recoveries since 1960. This is good news for borrowers, but some economists worry that the entry of China and other emerging countries into the global economy may have affected monetary policy in ways that central banks do not fully understand.

In its latest annual report, the Bank for International Settlements (BIS) asks whether it is really desirable to maintain positive inflation rates when China is boosting the world's productive potential so dramatically and thus reducing the prices of so many goods. In other words, are central banks targeting too high a rate of inflation now that China has joined the global market economy?

During the late 19th-century era of rapid globalisation, falling average prices were quite common. This "good deflation", which was accompanied by robust growth, is very different to the bad deflation experienced in the 1930s depression. Today, we would again have had "good deflation"—but central banks have instead held interest rates low in order to meet their inflation targets. The BIS frets that this has encouraged excessive credit growth.

This echoes a fierce debate in the 1920s. At that time, a similar jump in the world's productive potential (then caused by technology-driven productivity growth) was reducing manufacturing costs. Some economists suggested that, in such circumstances, overall price stability might be the wrong policy goal. Instead, they argued, average prices should be allowed to fall to pass the productivity gains on to workers and consumers as higher real incomes. But just like today, monetary policy prevented prices from falling. And an overly loose policy then inflated the late-1920s stockmarket bubble.

The Austrian school of economics offers perhaps the best framework to understand what is going on. The entry of China's army of cheap labour into the global economy has increased the worldwide return on capital. That, in turn, should imply an increase in the equilibrium level of real interest rates. But, instead, central banks are holding real rates at historically low levels. The result is a misallocation of capital, most obviously displayed at present in the shape of excessive mortgage borrowing and housing investment. If this analysis is correct, central banks, not China, are to blame for the excesses, but China's emergence is the root cause of the problem.

Not only has China's disinflationary impact caused low short-term interest rates, but China is also partly responsible for the low level of long-term bond yields. To keep its exchange rate pegged to the dollar, China was the biggest buyer of American Treasury bonds over the past year. In the first six months of 2005, its foreign-exchange reserves increased by more than $100 billion, to $711 billion, of which about three-quarters are in dollars. This has also kept capital costs artificially low.

Who calls the shots?

For many decades, global monetary policy has been set in Washington. When the Fed raised interest rates, global monetary conditions would tighten. Today, however, thanks in part to China's purchases of T-bonds, low long-term bond yields have offset the rise in American short-term interest rates over the past year. The yield on ten-year bonds is currently lower than before the Fed started to lift interest rates in June 2004. America's sovereignty over its monetary policy has therefore been eroded, with a given rise in short-term rates producing much less monetary tightening than in the past. To that extent, global monetary policy is increasingly being set in Beijing as well as in Washington.

By helping to hold down interest rates in rich economies, China may have indirectly created a global liquidity bubble. Total global liquidity last year rose at its fastest pace in three decades after adjusting for inflation. This excess liquidity has not pushed up conventional inflation (thanks to cheap Chinese clothes and computers), but instead it has inflated a series of asset-price bubbles around the world. Thus, pushing this argument to its limit, it could be said that the global housing boom is indirectly "made in China". Not only has China played a role in holding down short-term interest rates, but the People's Bank of China has also supported America's mortgage market by buying vast amounts of mortgage-backed securities.

What does the breaking of the yuan's peg to the dollar mean for bond yields? American Treasury yields rose by 12 basis points after Beijing made its announcement last week. Having played a hand in inflating America's housing bubble, could China now prick it by pushing up mortgage rates, which are closely tied to long-term bond yields?

If abandoning its dollar peg causes China to reduce its purchases of T-bonds, then yields will rise. But this depends on several uncertainties. For instance, will last week's revaluation reduce inflows of speculative capital into China, and hence its need to intervene in the foreign-exchange market by buying dollars? A large chunk of China's foreign-exchange intervention over the past year has been to offset not its current-account surplus but inflows of hot money. Some economists believe that, in the short term, the small revaluation will intensify speculation of further revaluations and so attract even more capital inflows, forcing the People's Bank of China to buy more Treasury bonds to stabilise its currency. If so, bond yields will remain low.

On the other hand, the switch from a dollar peg to a currency basket may cause China to diversify its reserves away from dollars. It is unlikely to dump its dollars, but it could well reduce its new purchases

of Treasury bonds in favour of other currencies. And, if China really has broken the yuan's link with the dollar, then this could be the trigger for another general slide in the greenback against the euro, the yen and other currencies, prompting investors to demand higher yields. The fate of American house prices could thus be determined by unelected bureaucrats in Beijing rather than the unelected central bankers of the West.

This article has argued that global inflation, interest rates, bond yields, house prices, wages, profits and commodity prices are now being increasingly driven by decisions in China. This could be the most profound economic change in the world for at least half a century. And its effect could last for another couple of decades. By some estimates, China has almost 200m underemployed workers in rural areas, and it could take at least two decades for them to be absorbed by industry. As this process takes place, it will continue to subdue wage growth and global inflation. Profit margins could also remain historically high for a period (though not for ever, as stockmarket valuations in many countries seem to imply).

China creates immense opportunities, but it also brings new risks. If it stumbles, or if it decides to buy fewer American T-bonds, pushing up yields, then America might really have something to complain about: the first global downturn made in China.

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Accounting

The ones that get away

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From The Economist print edition

Accounts are increasingly more art than science

IT IS corporate earnings season once again, and investors are poring over the numbers. This week, Sprint, an American telecoms firm, announced net profits more than twice as high as a year ago. Amazon, an internet retailer, revealed net income that had fallen by 32%, due, the firm said, to tax issues. The shares of both companies rose. Should they have done?

Profits figures are meant to shed light on how a company—and its stock price—might fare in the future. But many experts worry that increasingly they don't. The scandals at Enron and WorldCom—as well as more recent accounting snafus at General Electric and a big scam at AIG—show that accounting numbers are malleable. And they are getting squishier as the use of estimates in company accounts increases.

Whether this malleability is a problem is the subject of heated debate and carries with it important consequences. Reliable numbers mean that investors can make sound decisions. Bad ones lead not just to the inefficient allocation of capital but also to a loss of confidence in the markets and, when fraud is involved, to huge shareholder losses. A study by Glass Lewis, a research outfit, found that investors lost well over $900 billion in 30 big scams between 1997 and 2004.

Ever since accounting shifted from the simple tallying of cash in and cash out to “accrual accounting”, where profits and expenses are booked when incurred, forward-looking estimates have played a critical role in measuring company profits. This role has grown as “knowledge-based” economies have begun to replace the old widget-making versions, and businesses have become more complex.

The biggest boost to estimation, however, has come from the gradual shift to “fair-value” accounting. Before, assets and liabilities were mostly carried at their historic, original cost; “fair value” is an attempt to show their current worth. Fair-value numbers are up-to-date and arguably more relevant than their static but verifiable precursors. But they also result in more volatile profits and a heavier reliance on estimates for the many items (bank loans, buildings) that may not have a ready market.

Standard-setters on both sides of the Atlantic have been urging this shift. In June America's Securities and Exchange Commission, in a long-awaited report commissioned by Congress after the Enron scandal, also endorsed fair-value accounting, which it thinks will simplify accounts and reduce firms' interest in structuring transactions to meet accounting goals.

Others are less sanguine. Even with the best will in the world, estimates can be wildly off the mark. And they are easy to manipulate. In a recent study, Daniel Bergstresser and Mihir Desai of Harvard Business School and Joshua Rauh of the University of Chicago's Graduate School of Business found ample evidence of tinkering. At delicate moments—before acquisitions and equity offerings and exercising stock options, for example—some bosses inflated the assumed rate of return on pension-fund assets, thus flattering profits.

Baruch Lev of New York University's Stern School of Business, and Siyi Li and Theodore Sougiannis, from the University of Illinois at Urbana-Champaign, harbour a deeper worry: that estimates, which are supposed to improve the relevance of financial information by giving managers a means to impart their forward-looking views (on how many customers might return their new cars, for instance), are not very useful at all. That is, they do not really help investors to predict a company's future earnings and cashflows.

The three analysed 3,500-4,500 companies a year from 1988 to 2002. They then tried to “predict” future performance (earnings or cashflow) with five models in which historic cashflows and estimates were used to different degrees. The trio found that cashflows predicted future performance robustly, but adding estimates to them was little help in predicting future performance, or in generating returns from portfolios based on these predictions. It was a “sobering result”, they concluded.

Mr Lev blames this on the difficulty of making good estimates in a fast-changing, complex world as well as on a degree of earnings manipulation. “This is not to say we should toss the accounting system, which is overwhelmingly based on estimates, into the waste bin,” he says, “but it does point to the urgent need to enhance the reliability of accounting estimates—especially given the move to fair value.”

On this point, even proponents of fair value agree. The Financial Standards Accounting Board (FASB), America's standard-setter, is planning to release guidance on how to apply fair value later this year. It has devised a “hierarchy” of items according to how hard they are to value. At the top are items that have an observable price in a deep, liquid market (eg, listed corporate debt). In the middle are items where sophisticated valuation models are based on market inputs (eg, employee stock options). At the bottom are items where valuations are based wholly on management projections (eg, Enron's most esoteric financial instruments).

It is the lower end of the hierarchy that causes concern. “At this level, there is the risk that models can be used with prejudice,” says David Bianco of UBS, a Swiss bank. Regulators, too, are worried. Research by the Federal Reserve shows that the fair value of bank loans can swing widely depending on inputs and methodology. Market values for lower-rated corporate bonds, one possible benchmark, can vary by as much as 2-5%, giving managers leeway to fiddle with numbers.

The objective is objectivity

“Estimates are part of accounting. So the focus shouldn't be on the number of estimates,” argues Neri Bukspan, chief accountant at Standard & Poor's, a ratings agency, “but rather the objectivity and independence of those making the estimates and those tasked with verifying them.” This puts a greater onus on auditors to weed out good estimates from hyped ones—making their independence even more critical than it seemed after Enron. The Public Accounting Oversight Board, recognising this, also plans to expand its audit guidance on fair value.

Investors need to scrutinise the numbers harder, too. Better disclosure would help them. Mr Lev suggests that firms should say how much of key reported figures is based on facts (eg, revenues in the bag) and how much on estimates—a proposal that companies claim would tip their hand to competitors. But both FASB and its international counterpart are drafting standards requiring increased disclosure of how fair values are derived and their impact on profits and balance sheets.

Mr Lev has a more ambitious proposal. This entails forcing management to periodically “true up”—that is, disclose how their previous estimates have panned out. He argues that this would inject discipline into the system, allowing investors to penalise companies that consistently make bad estimates. Lynn Turner, a former chief accountant at the SEC, agrees. “Markets can't discipline without transparency.” Defenders of fair value say that this is confusing and unnecessary. A change in estimated value could be due to changing market conditions, not to a bad estimate. And fair-value accounting itself, some argue, is a constant “true up”. But then, there's “true” and true.

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Trade policy

Another such victory

Jul 28th 2005
From The Economist print edition

CAFTA squeaks through

Reuters

On their way

IN THE end, it enjoyed a majority narrower than the isthmus of Panama. Early on July 28th, the Central American Free Trade Agreement (CAFTA), which President George Bush signed more than a year ago, finally secured its passage through America's House of Representatives. Even as the bill was brought to the floor, the administration could not be sure it had all the yeas it needed. By the time the gavel fell, it did, 217 votes to 215. A gruelling experience, then. Was it a worthwhile one?

CAFTA is a modest agreement between a whale (the United States) and six minnows (five nations of Central America—Guatemala, Honduras, El Salvador, Nicaragua and Costa Rica—plus the Dominican Republic). The whale already admits about 80% of the minnows' exports tariff-free, and the Central American countries have already cut their average tariffs from around 45% in 1985 to about 7%.

Though the economic stakes were low, the politics were intense. Turn your backs on this agreement, congressmen were warned, and your country's Central American allies might opt instead for the "Bolivarian alternative". This rebel vision of a Latin America united against the gringos is named after Simón Bolívar, a 19th-century nation-builder, and espoused by Hugo Chávez, the leftist president of Venezuela.

But Mr Chávez in Caracas frightens America's congressmen rather less than the sugar and textile lobbies at home. In the end, Mr Bush's team had to resort to pettier sorts of persuasion. They won over several Republicans by promising that the linings and pockets of any garment stitched in Central America would be made from American fabric. Other hard-to-get congressmen will be rewarded with roads and bridges for their districts, opponents of the bill allege. On the eve of the vote, Mr Bush had to march up Capitol Hill in person to rally support to his banner.

Among the Democrats, precious few responded to this call. Any vestige of bipartisan trade consensus has faded. Some voted against the agreement in the name of the American worker. Others opposed it in the name of the Central American worker. They complain that some of the signatories to CAFTA fail to enforce labour standards laid down by the International Labour Organisation. Until they do, the United States should not trade with them.

Some Central Americans themselves are concerned. Farmers there still enjoy the shelter of high tariffs on certain goods, and would struggle to compete with duty-free imports from the United States. But

CAFTA's strictures do not apply to several sensitive crops, such as white corn and Costa Rican potatoes and onions. And the agreement gives other goods, including dairy products, up to 20 years to phase out protection. This should give farmers plenty of time to adjust, even if it deprives the poor of cheaper milk in the meantime.

In the end, Mr Bush carried the day despite substantial Democratic opposition. The victory he secured was small, but the defeat he avoided was massive. No president since Lyndon Johnson has suffered the humiliation of seeing Congress reject a trade deal he has negotiated. Indeed, some wonder whether America's dwindling band of free traders were wise to risk so much for so small a deal. But Mr Bush's trade team will take heart from this success for the bigger battles ahead.

The toughest fight of all will ensue should the “Doha round” of global trade talks ever reach a conclusion. Sadly, that is now in real doubt. In December, ministers from all the World Trade Organisation's members will meet in Hong Kong, where they are supposed to agree how to cut tariffs and subsidies, if not by how much. This week in Geneva, they and their deputies are trying to arrive at a “first approximation” of such an agreement for farm trade. But so far progress has been approximately nil.

If a Doha agreement ever reaches the House floor, the fight over CAFTA will seem a mere skirmish. But at the moment, it looks as if Doha's cause will be lost long before it reaches the Speaker's gavel.

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Italian banks

Fazio under fire

Jul 28th 2005 | ROME
From The Economist print edition

New controversy over Italy's contested bank bids

AP

The talkative Mr Fazio

IT SEEMED that it was all over bar the shouting. On July 22nd Spain's Banco Bilbao Vizcaya Argentaria (BBVA) abandoned its bid for Banca Nazionale del Lavoro (BNL). Three days later ABN Amro of the Netherlands said its attempted takeover of Antonveneta, another Italian bank, had also failed. The battle for control of these two mid-sized banks, which dragged on for four increasingly bitter months, appeared over, leaving Fortress Italy intact.

But more is now at stake. Antonio Fazio, governor of the Bank of Italy, is in trouble up to his eyebrows. Gianpiero Fiorani, the boss of a home-grown rival bidder for Antonveneta, Banca Popolare Italiana (BPI), is a friend of his. Leaked transcripts reported in the press of telephone conversations between the two tapped by government investigators suggest that the governor may have been less than neutral in his handling of the bids. There are now calls, predictably, for him to resign. On July 27th Consob, Italy's market regulator, suspended BPI's bid for Antonveneta as a "precaution". How did things go so wrong?

For a while, the Spanish and the Dutch looked well placed to breach Italy's banking establishment. The boards of BNL and Antonveneta had endorsed their bids. Mr Fazio had given them permission to increase their stake beyond 20%. And the EU Commission had approved both offers.

Yet behind the scenes, protectors of the banks' *italianità* mobilised their defence. Failing to convince one of Italy's big banks to step in as a white knight, they turned to weaker institutions. One was Unipol, a Bologna-based insurer. Unipol increased its stake in BNL to about 15%. It also recruited shareholders led by Stefano Ricucci and Francesco Caltagirone, two rich property developers, who had bought nearly 30% of the bank. On July 18th Unipol offered cash on the barrel for BNL, financed by a capital increase, debt and asset sales.

The other was Mr Fiorani's BPI, formerly known as Banca Popolare di Lodi. In spite of its anaemic finances, BPI launched two separate bids for Antonveneta, including an all-cash offer. This was after criminal investigations had been started into possible securities-laws violations.

It was in connection with these probes that telephone conversations were tapped. Mr Fiorani was delighted when Mr Fazio called him on July 12th to break the news—before making it public—that BPI's bid had got the go-ahead. According to Italian press reports of that particular chat, an emotional Mr Fiorani replied that he would kiss his friend "Tonino" on the forehead to thank him if he could. Mr Fazio himself may feel less warmly now.

Usually, a company has to prove that it has enough capital before its bid is approved, says Alessandro Roccati at Fox-Pitt Kelton, an investment bank. Analysts estimate that BPI was short about €1 billion ($1.3 billion) when it announced its offer.

In all this sorry mess, the only winners are the property developers who made some €900m from the sale of their stake in BNL to Unipol. The losers include Italian consumers, the country's reputation among foreign investors and, now, the credibility of Italy's central bank.

Italians pay their banks much higher annual fees and commissions than other Europeans. Opening an account can require filling out more than a dozen forms; closing one costs a hefty fee. Without foreign

competition, Italians will continue to be ripped off, says Davide Serra of Morgan Stanley, an investment bank.

Neither BBVA nor ABN Amro intends to remain a minority shareholder in its erstwhile target, so big chunks of capital will leave the country at a time when Italy's recession-hit economy desperately needs liquidity. ABN Amro's stake in Antonveneta is worth about €2.3 billion, and BBVA's shares in BNL would sell for around €1.2 billion.

Most damaging is the perception abroad of a chaotic tug-of-war between rogue investors, regulators and the judiciary. “We have generated a situation of enormous speculation under the motto ‘take the money and run',” says Luca Cordero di Montezemolo, head of the Confindustria, the employers' association.

Consob has ruled twice that BPI improperly acted in concert with other shareholders. Moreover, on July 25th, prosecutors confiscated the shares owned by BPI and ten investors (including Mr Ricucci), amounting to some 41% of Antonveneta's stock. If these shares were to come to the market, ABN Amro, which technically has control of the board now, could become the majority investor by buying its opponents' stakes. Yet having met with such hostility, the Dutch may turn their attention elsewhere.

This is not the end of cross-border bank mergers, says Armin Polster of Deutsche Bank, but banks are now likely to give Italy the same cold shoulder that they themselves received—at least until it's clear whether Mr Fazio should be in charge.

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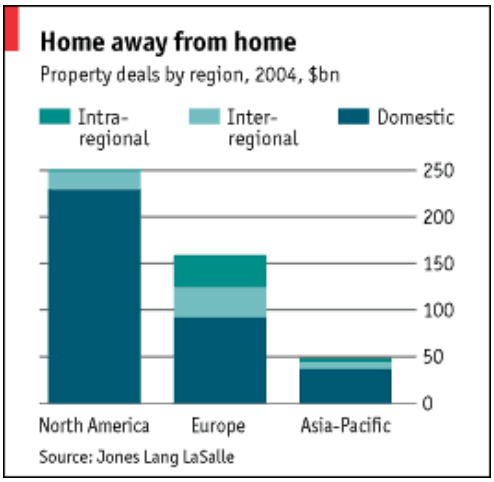
Cross-border property deals

Building up fast

Jul 28th 2005
From The Economist print edition

Property investors are increasingly ready to buy—and sell—abroad

WITH its transparent and liquid market, Britain has long been a favourite with non-European property investors. It still is. But for how long? These investors put $6.5 billion into British property last year, but sold $9.6 billion-worth. The same thing happened in the United States. Investors from outside North America bought $8.6 billion-worth of real estate there, but sold $11.6 billion. In contrast, they invested $1.4 billion in Canada, and sold almost nothing. Japan too was a one-way story: investors from outside the Asia-Pacific region put in $1.8 billion, but barely sold at all.



So, at any rate, says a new study from Jones Lang LaSalle, a global estate agency. Inevitably, the figures are heroic, mingling recorded deals with estimates of others. And pinning a nationality on investors is also brave in these days of easy and massive cross-border capital flows. So add a pinch of salt. But you won't find better.

Of the $99 billion of deals that crossed national frontiers in these three areas, inter-regional ones—where buyer, seller or both came from outside the region—accounted for $60 billion, if you count in $10.5 billion by Middle Eastern investors. That does not show (as the study argues) that investors ready to diversify across frontiers at all are likelier to go outside their “home” region. If all the people dealing in far-away buildings had been sellers, it would suggest just the opposite. In fact, sales did slightly outweigh purchases; North Americans took $3.2 billion, net, out of Europe, Europeans (less predictably, given the dollar's weakness last year) took $2.2 billion net out of North America.

But the figures do prove plenty of activity: that cross-border $99 billion in the three main regions is up from $82 billion in 2003. And it is over a fifth of the $457 billion, with purely domestic deals added in, that the study estimates as the grand total of property deals last year.

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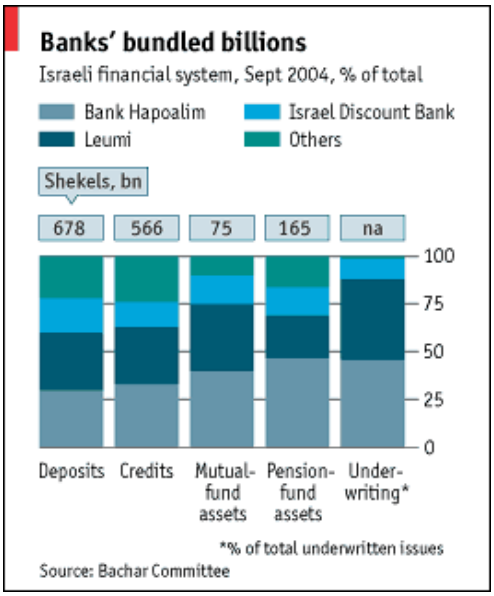
Israel's financial sector

Separate and lift

Jul 28th 2005 | JERUSALEM
From The Economist print edition

A step towards more competition

IN THE end there was nothing for the banks to do but watch as the surgeon's knife came down on them. This week the Knesset passed what is generally agreed to be the most far-reaching reform ever of Israel's capital markets. It forces the banks to sell off their provident and mutual funds; the two biggest, Hapoalim and Leumi, must do it faster than the rest and also reduce their holdings in insurance companies to 10%.



A few dominant players with a finger in virtually every pie (see chart) make Israel's banking sector a regulatory and competition-policy thicket. Banks provide some 95% of lending, compared with just 25% in the United States, according to Joseph Bachar, the director-general of the finance ministry and head of the reform committee. And they play a big role in pension savings, through their provident funds. In all sectors, the two big banks have the lion's share of the business. It is the sort of set-up that would make New York's attorney-general Eliot Spitzer see red.

Proponents of the reform, drafted last year, argued that it would both increase competition and put paid to an alarming list of conflicts of interest. For instance, because banks both advise on investments and manage mutual funds that do the investing, they have an incentive to (and, says the committee, mostly do) advise customers to choose the banks' own funds, when a rival fund might be better. And, in order to reduce their own lending risk, they may get their funds to invest in firms to which they lend money.

The banks, not surprisingly, were opposed. They grasped at an IMF report published in April, which said that the plan might go against trends elsewhere toward universal banking and that more conventional measures to open up the sector could meet the same objective. But a series of crises, including a money-laundering investigation into Hapoalim this year, turned both the government and the public against them. Bank owners were caught in a painful dilemma in April when their workers threatened to strike against the reform. In the end, they turned against the workers.

The reform's passage is a boost for Binyamin Netanyahu, the finance minister, as he tries to overhaul a creaking economy. Next he wants to open up the land market, which is 90% state-controlled, and to finish privatising Bank Leumi (this week the government sold off another 3.5%, to America's Citigroup, leaving 24.8% on its hands).

But though few in Israel oppose the Bachar reform, some say it does not go far enough. It may separate banks from their funds, but the same big names will dominate deposits and personal credit—which most of them administer with a legendary surliness of service.

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Japanese finance

The state as sugar daddy

Jul 28th 2005 | TOKYO
From The Economist print edition

Japan Post is only one state-owned financial outfit that needs reform

Bad for business
Japan's state-backed lenders
Loans outstanding, December 2004, ¥trn

Government Housing Loan Corporation	52.5*
Japan Finance Corporation for Municipal Enterprises	25.1
Japan Bank for International Co-operation	19.7
Development Bank of Japan	14.0
National Life Finance Corporation (SMEs)	9.9
Shoko Chukin Bank (SMEs)	9.8
Japan Finance Corporation for SMEs	8.0
Agriculture, Forestry and Fisheries Finance Corporation	3.3
Okinawa Development Finance Corporation	1.4

Source: Bank of Japan *As of March 2005

NO WONDER so many Japanese politicians are against privatising mammoth Japan Post. With ¥331 trillion ($2.9 trillion) in savings deposits and life-insurance assets, the country's "post office" has long allowed politicians to raise funds for favoured projects while hiding the true costs from taxpayers. To break this habit, Junichiro Koizumi, the prime minister, is risking his government on a drive to get a privatisation bill through parliament's upper house by mid-August.

As exhausting and nerve-racking as that effort has been, however, it is only one step towards unwinding Japan's pervasive system of financial socialism. There are nine other government financial institutions (GFIs), which lend to a wide range of special interests. These GFIs are sitting on ¥144 trillion of outstanding loans, and efforts to reform them have barely begun.

Heizo Takenaka, who has held several cabinet posts in Mr Koizumi's government and oversees most of his economic reforms, says that one of his next big jobs will be to tackle these state-backed lenders. The government has already made progress with one of them, the Government Housing Loan Corporation (GHLC), which once provided Japanese homeowners with cheap mortgages. In 2001 the government ordered it to stop making new home loans and to start securitising ones that were already outstanding. Over the past four years, the GHLC's loans have fallen from ¥77 trillion to ¥52 trillion. Private banks have increased their mortgage lending by roughly the same amount, so it seems clear that the state-backed lender had been crowding them out before.

That is also a problem with Japan's other eight GFIs. The tentacles of this financial octopus reach into every corner of economic life. Three of them compete to give cheap financing to millions of small companies. Another, the Development Bank of Japan, finances projects from urban railways to high-tech, and has involved itself in questionable bail-outs of badly-run companies. One GFI lends to municipal governments, utilities and other local projects; yet another to farmer-friendly causes; and the island prefecture of Okinawa, at the south-western end of Japan, has a special GFI of its own.

With Japan's private banks struggling to boost profitability, the last thing they need is a collection of big government lenders—backed by explicit and implicit subsidies—depressing lending rates and competing with them for business. And although, unlike the GHLC, Japan's other eight GFIs are also serving some

borrowers which no private bank would touch, much of that subsidised lending is arguably holding back economic growth, by channelling resources to inefficient firms with poor prospects.

Consider Japan's small companies. Throwing good money after bad might have made some sense in the late 1990s, as credit was getting tight and turning off the tap could have hurt the economy. Now Japan has the opposite problem. Its big banks are better capitalised and keen to lend. There are too many banking assets chasing too few borrowers, so corporate lending remains woefully unprofitable.

Moreover, a growing body of evidence suggests that propping up Japan's weakest firms has made it harder for healthier companies to hold down costs and boost revenues. If the government wants to provide a safety net for the millions of workers employed in small firms, it would do better to focus directly on the workers themselves.

Some of the GFIs' functions are worth keeping. The Japan Bank for International Co-operation (JBIC), for example, helps the government to administer its overseas aid, which most reckon is a useful role. But some of even JBIC's functions, such as export financing, might be usefully spun off.

Investors' knuckles will no doubt clench whiter over the next couple of weeks, as the vote on Japan Post approaches. But when it is done, either Mr Koizumi or his successor will have still more work to do.

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German bad loans

Augean stables

Jul 28th 2005 | FRANKFURT
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How local banks are learning the value of smelly business

GERMANY'S property and equity bubbles were never as inflated as Japan's, but they have nevertheless cast a pall over the German banking system. Now German banks are learning from the Japanese, among others, how to get the mass of non-performing loans off their balance sheets, and turn a pretty penny in the process. Shinsei Bank, the successor of Japan's defunct Long-Term Credit Bank (LTCB), recently formed a joint-venture with WestLB and Nord/LB, two publicly owned *Landesbanken*, to do just that.

Shinsei Bank's most visible shareholder is J.C. Flowers, an American fund manager that invests in distressed debt. In just five years, J.C. Flowers was able to transform financially crippled LTCB into one of Japan's most successful big banks.

For Shinsei's German venture, called SGK, the German banks will each put in €200m-worth ($240m) of bad loans and rely on J.C. Flowers to extract their residual value. With most dicey loans, there is either real-estate collateral to be seized or partial repayment to be negotiated with the borrower. As long as the gains from either outstrip the purchase price, the fund's investors are happy. This is work that the banks cannot or will not do themselves: calling in loans, managing property and severing relationships with customers is not their natural business.

J.C. Flowers was not the first American investment fund to enter the German bad-loan market, but it has been the first to offer German banks a share of the spoils. If Germany's competition authorities agree, SGK hopes to offer its platform to the entire public banking sector, which holds about a third of the estimated €300 billion of non-performing loans in the country's banking system. There are billions of profits to be made, especially by funds that can borrow up to three times their capital.

That kind of calculation has attracted many opportunistic investors to Germany. The market leader is Lone Star, of Dallas, Texas, which has bought loans with a face value totalling some €6 billion from German banks. That includes a €3.6 billion portfolio of real-estate loans from HypoVereinsbank and, partially in partnership with Merrill Lynch, an investment bank, €2.8 billion in loans from Dresdner Bank, part of the Allianz insurance group. Both of these big German banks needed to improve their capital position by getting uncertain risks off their balance sheet.

Dresdner Bank created a special institutional restructuring unit in 2002 to get rid of €35 billion of assets including unwanted foreign subsidiaries and bad loans. It hired a team from Sweden, which had performed a similar exercise after the Swedish banking crisis of 1992. After five years, the unit has nearly finished its task.

Dresdner has no plans to offer its loan-workout platform to banks with similar problems—a strange decision, given that its parent Allianz could make good money, like Lone Star and Goldman Sachs, an investment bank, by investing in the bad-loan business. These two firms clearly see a long-term future for the market in Germany. In June Lone Star bought Mitteleuropäische Handelsbank to allow it to handle live loans as well as non-performing ones—lending requires a banking licence. Goldman Sachs also gained a full banking licence by buying Delmora, the remains of two insolvent German banks.

J.C. Flowers is still looking for a German licence: in 2003 it tried to buy the troubled Bankgesellschaft Berlin, but its bid was rejected. Now it is interested in AHBR, a mortgage bank. Its joint-venture with Nord/LB and WestLB could provide another solution, however: SGK itself may apply for a banking licence in a year or two if business takes off.

Investors in bad loans are often seen as vultures, and they have certainly enjoyed rich pickings in Germany. Yet German bankers have been slow to develop an alternative. Deutsche Bank, for example,

has preferred to deal in more liquid single-name debt, such as Eurotunnel. Or it has “fronted”—acted as a bank for non-bank loan investors.

The normally dozy co-operative banks, ironically, have had their own workout solution since 1987 in the form of Bankaktiengesellschaft (BAG) Hamm. BAG Hamm is a reservoir of troubled loans, but it is a cost centre rather than a source of profit. The savings banks considered using this platform too, until SGK looked likely to embrace the entire public banking sector. Nevertheless, the savings banks in eastern Germany, where the bad-loan problem is acute, have suggested creating their own “bad” bank.

The concept that loan values can vary from par (100%) to zero has obviously taken hold, and it is changing the relationship between companies and banks. Last December KarstadtQuelle, a troubled retail and mail-order group, borrowed €1.75 billion from a syndicate of banks. The debt immediately appeared in the secondary market, at a hefty discount. The message is probably a healthy one: even in Germany, a company's relationship with its bankers has become a matter of hours, not years.

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Economics focus

It's the taking part that counts

Jul 28th 2005
From The Economist print edition

Are 5.1m Americans missing from the unemployment figures?

HOW strong is the American labour market? Around this time last year, few questions fascinated Washington more. Twelve months and one election later, much of the political heat has gone out of the issue. In June, unemployment fell to 5%, the lowest rate since September 2001. In what may be his last report to Congress as chairman of the Federal Reserve, Alan Greenspan warned legislators that the "slack" in the labour market was being taken in, and that unit labour costs had "turned up of late".

A new paper* by Katharine Bradbury of the Federal Reserve Bank of Boston should keep the question open for a while longer. The unemployment rate, she suggests, may be a poor measure of slack in the labour market. By her yardstick, there may be as many as 5.1m Americans who do not appear in the unemployment rolls, but who might rejoin the job queue if work were more forthcoming. If so, the "true" unemployment rate could be over 8%, not 5%; the true number of jobless 12.6m, not 7.5m.

Looking for work is a full-time job. Many job-hunters quit, despairing of ever landing their quarry. Some of these "discouraged workers", as economists call them, fall back on the earnings of a partner or spouse, some go back to school, others discover disabilities that qualify them for government benefits. Since they have dropped out of the labour force, they also drop out of the unemployment numbers.

They show up instead as declines in the "labour-force participation rate". These falls have been quite striking since the 2001 recession. In March of that year—the month the economy peaked—67.2% of Americans over 16 years of age either had a job or sought one. For the past 18 months or so, the figure has hovered stubbornly around 66%, refusing to recover even as output has rebounded. The difference may seem small—only one percentage-point or so. But that is 1.2 out of every 100 adult Americans, or more than 2.7m people.

In past recoveries, all but the most discouraged workers had taken heart by now, tempted back into the labour force by rising jobs and wages. What is different this time around? Ms Bradbury digs deeper among the discouraged, sifting their numbers by age and by sex. In this upswing, it seems, the young and middle-aged are uncharacteristically work-shy, but the elderly are rolling up their sleeves in surprising numbers. If this recovery had followed the pattern set by the previous five, she calculates, another 5.1m Americans under 55 years of age would be in the workforce by now. But 3.4m Americans over that age would not be. The shortfall in young and middle-aged workers is partly offset by a windfall of older workers. This raises two critical questions: will the missing millions under the age of 55 enter the workforce in due course? And will those over 55 stay?

Goodbye or au revoir?

To the second question, Ms Bradbury answers in the affirmative. The industriousness of the elderly has little to do with a jobs boom and more to do with the baby boom, she argues. The first of the post-war baby boomers turned 55 in the past few years. Thus the over-55 age group is unusually "young" at the moment, containing a bulge of people at the lower end of the age range. Eventually, of course, the baby boomers will retire. But there is no reason to think they will drop out in the next year or two.

The answer to the first question is less certain. The 2001 recession interrupted the longest expansion in post-war history. In that golden age, students cut short their studies, the elderly deferred their retirement, criminals hung up their swag bags—everyone showed up for work in the new economy. Peaks that high may never be scaled again, Ms Bradbury points out. If so, some of the 5.1m Americans she thinks are missing from the labour force may be gone for good.

The other mystery is women. During the four decades from the 1960s, women have been marching into America's labour force in ever greater numbers. Their participation rate showed an upwards trend which the occasional recession would slow or flatten, but not reverse. This meant that three or four years into a normal recovery, the female participation rate would not only regain its pre-recession peak, it would surpass it.

Women play a large role in Ms Bradbury's calculations. Almost 4.1m of her 5.1m missing workers are female. But this enormous gap assumes that the 40-year trend of rising female participation should have continued apace. In particular, it implies that the female workforce should by now be almost 2.2m larger than it was even in March 2001.

Ms Bradbury is quick to concede that this assumption may not hold. With about 60% of women already participating in the job market, their long march into work may be drawing to a close. From now on, the female workforce may grow and shrink with the ups and downs of the economy, much as the male workforce does. Under this scenario, perhaps only 1.3m of the missing 4.1m women should have been expected to return to the workforce as the economy picks up. This would leave a less spectacular shortfall of 2.3m, not 5.1m, workers overall.

If Ms Bradbury is right, then full employment in America is a more distant goal than it currently appears. Her calculations also imply that the economy can continue to grow apace for some time before the Fed needs to worry about labour shortages, wage hikes and inflationary pressure.

Mr Greenspan himself, of course, is due to drop out of the labour force in January of next year, a month or so shy of his 80th birthday. It will fall to his successor to decide whether the labour force's missing millions need coaxing out of their more premature retirement.

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* “Additional slack in the economy: the poor recovery in labour force participation during this business cycle”, Federal Reserve Bank of Boston.

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AIDS

No carnival

Jul 28th 2005 | RIO DE JANEIRO
From The Economist print edition

AP

AIDS treatment is more widely available than ever—but efforts are needed to stop people becoming infected in the first place

Get article background

CUTTING bits of healthy tissue off a human body is not normally recommended. People evolved into human form for a reason, so it is probably best left alone unless there are good arguments for messing with it. But in the fight against AIDS, anything is worth a try—even circumcision. And, according to a trial whose results were announced at the latest international meeting on AIDS, circumcision works. Indeed, it works so well that the trial's organisers, France's National Agency for AIDS Research (ANRS), felt obliged to stop it half way and tell all the participants, so that those in the control group could get circumcised, too.

The Third Conference on HIV Pathogenesis and Treatment, to give its full name, is a reaction to the huge international AIDS conferences that are held every two years. Those meetings, which started as scientific workshops, have become jamborees and platforms for activists to bite the hands of the donor governments and drug companies that feed them. The International AIDS Society, which is responsible for organising them, thus decided to fill the gap-year with a purely scientific meeting, give it a long-winded and off-putting title, and hope that the activists wouldn't notice. In this it has, by and large, succeeded.

But even scientists like a dose of excitement and Bertran Auvert, the head of the ANRS trial, administered this conference's fix of that particular drug. It has been suspected for two decades that circumcision might protect against AIDS. At first, this was because infection rates in areas where the practice is routine are often far lower than in apparently similar places where it is not. Subsequently, it was found that the foreskin is rich in cells whose surfaces are covered with proteins that allow HIV to lock on to them and force its way inside. And after that, a number of direct comparisons of the circumcised with the uncircumcised suggested the procedure really was effective.

But looking at those who have been cut because they or their parents chose it is no substitute for a proper clinical trial that cuts or does not cut its participants at random. The ANRS study, one of four such trials begun in Africa a couple of years ago, grasped the bull by the horns. It took a group of uncircumcised and uninfected South African volunteers and gave half of them the snip. By the time the trial was stopped it was apparent that for every ten uncircumcised men who had become infected, only three of the circumcised had succumbed, even though only half of the volunteers had at that point participated for the full 21 months originally envisaged.

Dr Auvert's trial—which, everyone was keen to emphasise, needs to be backed up by others—is part of a reaction against the prevailing ethos of AIDS, which is to treat it rather than prevent it. As Bernhard

Schwartländer, of the Global Fund to fight AIDS, Tuberculosis and Malaria, observes, prevention has no lobby. Only those already infected become activists. But only prevention will stop the epidemic.

The past few years have, indeed, seen the treatment campaign against AIDS accelerate. The distribution in poor countries of anti-retroviral drugs, which keep the symptoms of AIDS at bay, is proceeding apace. Admittedly, it is not going at the pace that the World Health Organisation would have liked. The WHO's bosses wanted 3m people to be on these drugs by the end of this year, but that number will not be achieved until the end of 2006.

In this game, however, if you hit your target on time it probably was not ambitious enough. Anyway, the G8 meeting in Britain earlier this month provided a new target. The meeting's participants announced they were “aiming for as close as possible to universal access to treatment for all those who need it by 2010”.

Admittedly, this bold objective includes the weasel phrase “as close as possible”, which provides useful political wriggle room. But it is still a hostage to fortune, and one that AIDS activists, not known for their reticence, are likely to keep reminding governments about. Indeed, Jim Kim, head of the WHO's HIV and AIDS programme, got the ball rolling by telling the meeting's participants that it was now up to them to come up with a “road map” that would allow the G8 aim to be met. He wanted that map, he said, before next year's World Health Assembly in May.

There is a risk, though, that if drug-delivery programmes are rolled out willy-nilly without accompanying transmission-prevention programmes, they will eventually make the situation worse. This risk is the object of furious debate, not least because there are very few data. But it is plausible enough to worry about, and it comes in two parts. The first is that sloppy adherence to drug-taking regimes will cause drug-resistant viruses to emerge. The second is that those on drugs, feeling themselves to be better—and even, possibly, immune to further infection—will engage in the sorts of risky behaviour that infected them in the first place. Several mathematical models discussed at the conference suggest that, without a parallel advance in prevention techniques, the spread of effective treatment might even increase the spread of the virus.

One way to combat this risk is to use the network that is being put into place to deliver treatment to preach the message of prevention. Another, which is just as important, is to find out which prevention techniques actually work. There is still, for example, argument about whether it was the wider use of condoms or a reduction in promiscuous sex that curbed the epidemic in Uganda, even though that curbing is held up as one of the successes of the global anti-AIDS programme.

At the moment, condoms and fidelity are indeed the only prevention techniques around (unless like the American government, but unlike most workers in the field, you regard preaching abstinence as a sensible option). And, until recently, there was little prospect of that changing. As Dr Schwartländer said, prevention has no lobby. The trials are long-winded, as they have no clear end. They rarely involve patented (and therefore lucrative) products, so industry is loth to pay for them. And they require huge numbers of participants to get a statistically meaningful result.

Nevertheless, trials of new techniques for preventing transmission are starting to happen. A vaccine, sadly, seems as far away as ever. But, besides the circumcision trials, there are trials on the infection-preventing qualities of cervical diaphragms, on a vast range of vaginal microbicides (not all of which also act as contraceptives), on acyclovir (a drug that suppresses genital herpes and, with it, the sores that give HIV access to the bloodstream) and on tenofovir (a drug that is used to treat HIV infection and is now being tested to see if it can act as a prophylactic). Several of these trials are expected to report in 2007, just in time for the next meeting.

New prevention techniques will not be a panacea. In particular, if they do not provide 100% protection, they risk encouraging risky behaviour that would spread the virus. But if used sensibly, they should help to stop transmission in a way that treatment never can. Perhaps, therefore, the organisers should change the name to the Conference on HIV Pathogenesis, Treatment and Prevention. By 2007, the P-word might even be fashionable.

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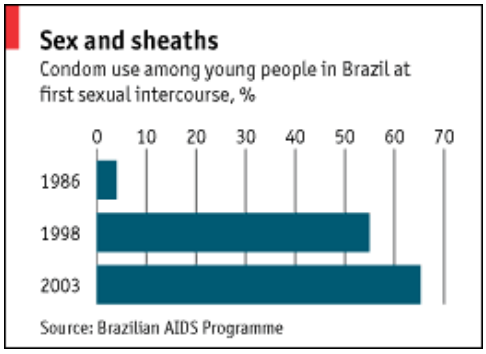
AIDS in Brazil

Roll out, roll out

Jul 28th 2005 | RIO DE JANEIRO
From The Economist print edition

What can the world learn from Brazil's experience of dealing with AIDS?

Get article background

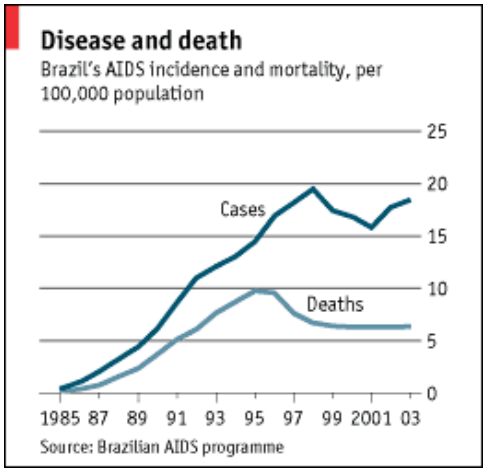

Sex and sheaths
Condom use among young people in Brazil at first sexual intercourse, %
0 10 20 30 40 50 60 70
1986
1998
2003
Source: Brazilian AIDS Programme

IT IS no coincidence that Rio de Janeiro was chosen to host this year's Conference on HIV Pathogenesis and Treatment. Brazil's handling of the epidemic is widely regarded as exemplary. In the early 1990s, the World Bank predicted that, by 2000, HIV would have infected 1.2m Brazilians. Today, five years after that deadline, the total is just half the Bank's prediction—about 600,000. So how did Brazil do it, and can other poor countries learn from what was done?

Perhaps the first lesson is don't be squeamish. Brazil, a predominantly Catholic country, hands out free condoms in abundance. Some 20m are given away every month—a figure that is boosted by 50% in February to accommodate the exuberance of the country's famous carnivals. Drug users, too, are treated sensibly. Those who inject are offered regular supplies of clean needles and, as a result, three-quarters of them claim never to share needles with others. Nor are prostitutes neglected. Both ladies and gentlemen of the night are the targets of campaigns intended to promote condom use.

The second lesson is treat freely. Brazilian law gives all residents the right to the best available drug treatment at no cost. This is important, because having to pay discourages people from complying with the full treatment and thus encourages the emergence of drug-resistant viruses. Providing free treatment is, of course, expensive. This year, the government will spend $395m on anti-HIV drugs, almost two-thirds of it on three expensive patented drugs. This has brought it into conflict with foreign drug companies. Although it has never actually broken a drug-company patent, the government has exploited every available loophole to evade patents and buy or manufacture generic versions of drugs. For those patents that cannot legally be evaded, the government has played chicken with the patent-owners over prices, knowing that manufacturers are desperate to avoid a patent-breaking precedent that others might follow. So far, it has been the companies that have blinked, though the latest staring match, with Abbott Laboratories, an American firm, over a drug combination called Kaletra, has yet to be resolved.

The third lesson is to encourage voluntary action. In 1992, Brazil had 120 charities and voluntary groups devoted to AIDS. By the turn of the century, that had risen to 500. The virtues of voluntarism were recently confirmed when the Global Fund (the main multilateral distributor of anti-AIDS money to poor countries) audited the success of its donations. It found that spending by voluntary groups usually produced the best value for money.



The fourth lesson is to do the sums. One of the arguments that has sustained Brazil's anti-AIDS programme is "if you think action is expensive, try inaction". The government spent $1.8 billion on anti-retroviral drugs between 1996 and 2002 but estimates that early treatment saved it more than $2.2 billion in hospital costs over the same period. Add that to the GDP loss that Brazil would have suffered if the World Bank had been right, and an aggressive programme of prevention and treatment does not seem so costly after all.

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Environment

Down with trees

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Planting trees can exacerbate drought and fail to tackle climate change

Get article background

CONVENTIONAL wisdom says trees are good for the environment. They absorb carbon dioxide—a greenhouse gas—from the atmosphere and store it as carbon while releasing oxygen, a process for which forests have been dubbed “the lungs of the planet”. The roots of trees have been thought to trap sediments and nutrients in the soil, keeping nearby rivers free flowing. Trees have also been credited with steadying the flow of these rivers, keeping it relatively constant through wet and dry seasons, thus preventing both drought and flooding. Pernicious nonsense, conclude two pieces of research published this week.

The first, a four-year international study led by researchers at the University of Newcastle, in Britain, and the Free University of Amsterdam, identifies several myths about the link between forests and water. For example, in arid and semi-arid areas, trees consume far more water than they trap. And it is not the trees that catch sediment and nutrients, and steady the flow of the rivers, but the fact that the soil has not been compressed.

The World Commission on Water estimates that the demand for water will increase by around 50% in the next 30 years. Moreover, around 4 billion people—one half of the world's population—will live in conditions of severe water stress, meaning they will not have enough water for drinking and washing to stay healthy, by 2025.

The government of South Africa has been taking a tough approach to trees since it became the first to treat water as a basic human right in 1998. Trees lose water through evaporation (the technical term is transpiration) at twice the rate of grassland or South Africa's unique fynbos scrubland. In a scheme praised by the hydrologists, the state penalises forestry companies for preventing this water reaching rivers and underground aquifers.

In India, large tree-planting schemes not only lose valuable water but obfuscate the true problem identified by the hydrologists: the unregulated removal of water from aquifers to irrigate crops. Farmers need no permit to drill a borehole and, as most farmers receive free electricity, there is little economic control on the volume of water pumped. In the Kolar district in Karnataka, wells have dried up as the water table has plummeted from six metres to 150 metres below ground.

The report—“From the mountain to the tap: how land use and water management can work for the rural poor”, which is published by Britain's Department for International Development—concludes that there is no scientific evidence that forests increase or stabilise water flow in arid or semi-arid areas. It recommends that, if water shortages are a problem, governments should impose limits on forest plantation.

The second piece of research looked at how long the forests of the Amazon basin cling on to carbon. Growing trees consume carbon dioxide and it was thought that only when the tree died, perhaps hundreds of years later, would the carbon be returned to the atmosphere. No such luck. In a paper published in *Nature* this week, a team of American and Brazilian scientists found that trees were silently returning the carbon after just five years.

Before taking an axe to trees, however, consider the merits of the tropical rainforests. In Costa Rica, the upland cloud forests of the Arenal National Park trap water from clouds while losing little through transpiration. Water flowing from the forest feeds hydroelectric plants that provide a third of Costa Rica's electricity needs. It then irrigates farmland and drains into an important wetland that hosts migratory birds, before flowing into a hugely fertile fishery. The area has now become a prime

destination for eco-tourists, Costa Rica's largest source of foreign exchange.

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The neurology of consciousness

Crick's last stand

Jul 28th 2005
From The Economist print edition

Francis Crick suggests where to find the seat of consciousness

IT IS traditional to begin an article about Francis Crick by quoting his collaborator, James Watson, who wrote, “I have never seen Francis Crick in a modest mood.” The immodesty that carried Crick to the discovery of the structure of DNA in 1953 clearly never left him. His latest paper (and his last, for he died in 2004) proposes to explain, of all things, the neurological basis of human consciousness.

Mechanistic explanations of consciousness are hard to come by because consciousness is so poorly understood. Indeed, it is one of the few unexplained phenomena that are genuinely mysterious rather than merely problematical. But Crick, together with his long-time collaborator Christof Koch, of the California Institute of Technology in Pasadena, focused on a part of the mystery that seems tractable. This is the integrated nature of conscious sensation.

As the two researchers put it in their paper, which was published this week in the *Philosophical Transactions of the Royal Society*, “When holding a rose, you smell its fragrance and see its red petals while feeling its textured stem with your fingers.”

The part of the brain that caught the two researchers' interest is the claustrum, a thin sheet of grey matter that lies concealed beneath part of the cortex (the outer covering of the brain that carries out the computations involved in seeing, hearing and language).

The key to the researchers' claim is that most, if not all, regions of the cortex have two-way connections to the claustrum, as do the structures involved in emotion. It is plausible that the smell, the colour and the texture of the rose, all processed in different parts of the cortex, could be bound together into one cohesive, conscious experience by the claustrum. The authors liken it to a conductor who synchronises and co-ordinates various parts into a united whole.

Thus far, this is mere anatomical speculation fuelled by the fact that very little is known about what the claustrum actually does. Crick hoped that his final paper would inspire researchers to begin to develop molecular techniques to disable the claustrum in animals to observe the aftermath. Time will tell whether Crick's spectacular contribution to understanding genetics will be replicated in the sphere of consciousness.

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New fiction

Not a pretty sight

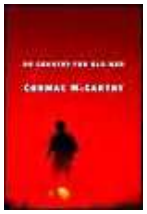
Jul 28th 2005
From The Economist print edition

But one that should hit the jackpot, again

CORMAC MCCARTHY'S 1992 National Book Award winner “All the Pretty Horses”, a saga about three Texan boys' ill-starred horseback trek across the Mexican border in 1948, attracted a broad, passionate readership. With lyrical descriptions of landscape and terse, unpunctuated dialogue, a distinctive voice powered a gripping story. Yet a subset of “Pretty Horses” fans has been disappointed by many of Mr McCarthy's other westerns, written both before and after the award-winning novel. Take his 1985 tale of violent bounty hunters, “Blood Meridian”. Prose that for hardcore McCarthy enthusiasts is thundering and eloquent reads to the more fastidious as turgid and pretentious.

Good news for this latter cadre: “No Country for Old Men”, Mr McCarthy's ninth novel, has much of the same resonance, luminosity and narrative thrust of the book that put its author so firmly on the literary map.

No Country for Old Men
By Cormac McCarthy



Knopf; 306 pages; $24.95.

Buy it at
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In 1980, Llewelyn Moss, a working-class welder in Mr McCarthy's established territory of southern Texas, trips over the detritus of a drug deal gone bad—a smattering of dead bodies, a trunk-load of heroin, and $2.4m in cash. He knows that if he takes the money it will change his life, and probably not for the better. He may even have a presentiment that it will end his life. But he takes it anyway. Thus the stuff of prime-time cop shows is transformed into a Faulknerian moment. One senses that Llewelyn is motivated less by greed than by a determination to pick up what fate has thrown in his path like a gauntlet.

Thereafter, Llewelyn is on the run from an ex-Special Forces agent hired by the cartel that wants its money back, an icy psychopath who murders anyone in his way in the spirit of picking his teeth, and a county sheriff named Bell, who forms the moral centre of the novel. Bell is as driven to rescue Llewelyn from his fate as the welder is driven to meet it.

Perhaps because the prose is so poetically pared down, Mr McCarthy's quirks of grammar and punctuation are less irksome than in some of his earlier works, in which the absence of quotation marks, for example, can make dialogue difficult to discern. That said, it is still challenging to understand why “dont” merits no apostrophe, while “I'd” and “that's” do; why “Texas” is awarded a capital letter, but not “spanish”. Leaving aside the issue of affectation, the puzzle is distracting.

The momentum of the plot, mainly written in the third person, is slowed by reflective, sober passages in the first. While Bell's down-home, under-educated voice sometimes slips—it strains credibility when our county sheriff refers to “mercantile ethics”—in the main his entries are some of the most mournful, moving sections of the book. He is bewildered that, “We're being bought by our own money. And it aint just the drugs. There is fortunes bein accumulated out there that they dont nobody even know about. Money that can buy whole countries...But people dont just up and decide to dope themselves for no reason. By the millions.” He offers nuggets of rough-hewn wisdom: “I think sometimes people would rather have a bad answer than no answer at all.”

“All the Pretty Horses” had a timelessness about it, and could almost have taken place 100 years earlier with little changed. By contrast, “No Country for Old Men” is rooted in the corruptions of the modern-day border—the world of human trafficking, drug smuggling and sex slavery, against which Bell fights his losing battle.

“He'd felt like this before,” writes McCarthy of his hero, “but not in a long time and when he said that he knew what it was. It was defeat. It was being beaten. More bitter to him than death. You need to get over that, he said. Then started the truck.” For Bell, moral breakdown “starts when you begin to overlook bad manners,” because “any time you quit hearin Sir and Mam the end is pretty much in sight”, leading to bodies in the desert surrounded by brick-sized parcels of heroin.

Nevertheless, both Bell and Llewelyn pulse with a deep wonderment at the miracle of their own fine marriages, keep an irrationally abiding faith with the very values of which they see such little evidence in the contemporary American west, and gape in quiet amazement at the mystery of it all. This is a dark book, but its protagonists have soul.

No Country for Old Men.
By Cormac McCarthy.
Knopf; 306 pages; $24.95.
To be published in Britain by Picador in November

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Rudolph Giuliani

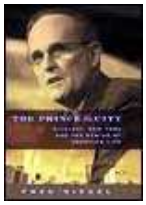
America's mayor

Jul 28th 2005
From The Economist print edition

THE calm unyielding (yet racially and religiously inclusive) leadership of Rudolph Giuliani on September 11th 2001 transformed the mayor of New York into a national hero, dubbed “America's mayor” by Oprah Winfrey. To the outside world—then, as now, underwhelmed by the president of the explosion-shocked superpower—Mr Giuliani came to symbolise all that was most impressive about America's response to the terrorist attacks. His heroism during the crisis has made “Sir” Rudy (he was knighted in 2002 by Queen Elizabeth) a potential candidate for the presidency in 2008. Yet it was but the remarkable final act of an eight-year reign in City Hall that required leadership just as heroic in much less obvious ways.

In Fred Siegel's gripping and persuasive account of that reign, Mr Giuliani mostly comes across as the opposite of the unifying figure standing amid the ruins of the World Trade Centre. According to this modern retelling of Machiavelli's “The Prince”, Mr Giuliani revived a city in seemingly irresistible decline by the determined application of a “corrupt wisdom” that confronted the conventional wisdom propagated by New York's powerful interest groups (above all, the public-sector unions and Manhattan liberals). Strikingly, Rudy's favourite aphorism, “I'd rather be respected than loved,” echoed Machiavelli's “it is better to be feared than loved”.

The Prince of the City: Giuliani, New York and the Genius of American Life
By Fred Siegel



Encounter Books; 408 pages; $26.95

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After a thoroughly nasty election campaign, in which Mr Giuliani was portrayed by his Democratic opponents as a racist and (almost as bad in New York) a Reaganite, he defeated the incumbent, David Dinkins, the city's first African-American mayor, by only 50,000 votes in November 1993. Under Mr Dinkins, New York had come to be seen as ungovernable: rife with crime; beset with social problems that required massive welfare spending; with an infrastructure that was literally falling apart; and dependent on huge financial handouts from the federal government.

Mr Giuliani proved that the city had merely been misgoverned. Mr Dinkins had pursued a “liberal” policy agenda based, as Mr Siegel describes it, on throwing money at problems while tolerating anti-social behaviour in all its forms. Mr Giuliani, a believer in the “reinventing government” policies that had helped revive other troubled cities, set about imposing budget discipline, encouraging private-enterprise, raising educational standards, getting welfare recipients back to work and, above all, ridding New York of crime.

AFP

Prince Rudy's city

New Yorkers who backed Mr Dinkins over Mr Giuliani now like to claim that the policies that slashed crime were already coming in when Rudy took office. Mr Siegel shows that Mr Giuliani really does deserve the credit. Police numbers were rising under Mr Dinkins, but that would not have done much without Rudy's “broken windows” and “zero tolerance” policies of cracking down on minor crime on the correct assumption that the “small” criminals were also doing most of the nastier crime.

Ironically, Mr Giuliani's war on crime went so well that in 2000 New Yorkers began to complain that the police had too much power. Mr Giuliani's typically abrasive response to such talk inflamed his critics, prompting a plunge in his popularity that continued until September 11th.

The Prince of the City: Giuliani, New York and the Genius of American Life.
By Fred Siegel.
Encounter Books; 408 pages; $26.95

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Poland

Brave women, but not sisters

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WHEN General Wojciech Jaruzelski imposed martial law in Poland on December 12th 1981, most of the male leaders of the trade union Solidarity were imprisoned. It was women who kept the organisation going. They dodged the secret police, forged papers, gave underground seminars and produced a clandestine mass-circulation newspaper, which the authorities repeatedly, but vainly, tried to suppress. Their chauvinism meant they assumed that the conspirators they were seeking must be men. During house searches, the secret police would usually neglect to investigate anything connected with women or children. Consequently, piles of nappies became one of the most preferred hiding places.

These women had been largely invisible beforehand, and mostly shunned publicity after Communism fell. Their story is fascinating and untold. Much of the excitement of those years, and the gutsy genius of the women of the *Damska Grupa Operacyjna*—or Women's Operational Group, a name that parodied secret-police jargon—comes across in Shana Penn's book. But this is despite her efforts, rather than because of them. Steeped in the parochial thinking of American academic feminism, she devotes too much space to the (to her) mystifying puzzle of her heroines' lack of gender consciousness. Surely they should realise that as women battling male structures, they were feminist pioneers?

Solidarity's Secret: The Women Who Defeated Communism in Poland
By Shana Penn

University of Michigan Press; 372 pages; $34.95

Buy it at
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There is a lot in Poland for an American feminist to get cross about. But Ms Penn struggles, and mostly fails, to make the imaginative leap necessary to see that her subjects' preoccupations were different. Joanna Szczesna, a magnificent activist to whom Ms Penn devotes considerable space, has complained about the author's dismay that the women did not gain their share of the political fruits of victory: “It happened that once in my life I put out lots of fires, but it was not because of gender discrimination that I didn't become a fireperson. I didn't become one because I didn't want to be one.”

Ms Penn makes some effort to mention the role of womanhood in romantic Polish nationalism, such as the idea of the *Matka Polka* (Mother-Pole), a heroic, tragic figure who must send her sons to die for the country's liberation. But she doesn't really approve (nationalism, in her world, is highly suspect). And she fails to understand the importance of the Roman Catholic Church in Poland. She makes a few dismissive references to the “cult of the Virgin Mary”, but no attempt to reflect its symbolism or theology.

Ms Penn also displays carelessness in failing to respect one interviewee's request for anonymity. This person appears under a pseudonym in the main text, but under her real name in the index.

However, the greatest problem is that although Ms Penn realises she is talking a different language, she cannot adapt. She writes plaintively that her subjects “had very different understandings of ‘internationalism', ‘leftist politics', ‘feminism' and ‘collaboration'. For many of them, these words held immediate, negative associations with Communism, and when I used them they made people wince or fume...my choice of language sometimes made me appear either highly suspect or incredibly naive.” Quite so.

Solidarity's Secret: The Women Who Defeated Communism in Poland.
By Shana Penn.
University of Michigan Press; 372 pages; $34.95

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Second world war

Justice stained

Jul 28th 2005
From The Economist print edition

WILLIAM JOYCE was not British, but wished he was. Despite being, in his own eyes, an ultra-patriot, he spent the war broadcasting for the Nazis. At the end of it, he was hanged for treason. Oddly, he made no attempt to use in his defence his links with the British intelligence service, which had persisted even during the war.

There are many mysteries and puzzles about Joyce's life, some solved in Nigel Farndale's new biography, others just ably investigated. They stretch across the three acts of what he provocatively, but rightly, calls a tragedy. The first takes place in the seedy, cranky world of pre-war British fascism, where Joyce's intellectual brilliance and rhetorical skills made him a big fish in a pool ill-stocked with talent.

From a present-day viewpoint, it seems almost incomprehensible that anyone but the most thuggish anti-Semite would find Nazism attractive. But the author paints a skilful and convincing picture of an era when there was a widespread feeling that the existing political and economic system had failed; that Germany and Italy offered an attractive alternative, and that appeasing Hitler was not only sensible, but right.

Another puzzle is Joyce's relationship with Maxwell Knight, the nutty head of a British intelligence outfit that both infiltrated, and sympathised with, the far right. Amazingly, as war loomed, Knight tipped Joyce off that he was about to be arrested, allowing him to escape to Germany.

The second act is set in Berlin, where Joyce and his wife Margaret became the kingpins of the Nazis' English-language propaganda machine. Joyce's war-time broadcasts had a huge audience in Britain—where he was known as Lord Haw-Haw—not least because the BBC, particularly at the start of the war, was so stodgy and secretive. Mr Farndale captures war-time Germany's descent from triumph to panic, and the mundane details of the Joyces' rackety marriage (they divorced, remarried, had countless affairs, and spent a lot of time getting drunk).

The third act comes after Joyce's capture, when the British tried to work out how they could prosecute a foreigner for treason. Born in America of Irish parents, he had falsely obtained a British passport, but then become a naturalised German citizen. Even with a specially designed new treason law, the case was flimsy, resting on the assertion that the user of a passport owed loyalty to the country issuing it.

Mr Farndale surmises, probably rightly, that Joyce's failure to mention his relationship with the intelligence services during his trial meant that the authorities had cut a deal with him; they would let Margaret go free, if he kept mum. If so, it was as shabby as everything else. His appeal was turned down, the judge said later, because of what the public would think.

But for some repetition, this biography is a model of its kind. It rests on thorough research while displaying intuitive understanding of the subjects' personalities. The moral landscape is painted with scrupulous fairness. By the end, the reader is close to sympathising with the revolting Joyce, facing death with dignity, rather than with the cowardly, vengeful officialdom of the country he so revered.

Haw-Haw: The Tragedy of William and Margaret Joyce.
By Nigel Farndale.
Macmillan; 374 pages; £20

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By Nigel Farndale

Macmillan; 374 pages; £20

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"Charlie and the Chocolate Factory"

A chocolate yellow brick road?

Jul 28th 2005 | LOS ANGELES
From The Economist print edition

A definitive remake of a children's tale

TIM BURTON'S "Charlie and the Chocolate Factory" is the second film adaptation of Roald Dahl's 1964 children's book, made as "Willy Wonka and the Chocolate Factory" in 1971. Spectators of a certain vintage, with fond memories of the book or the film will be on guard against Mr Burton's twisting of the tale. But this new version, now playing in America and opening in Europe from this weekend, is likely to become the definitive one, a Wizard of Oz for the new millennium.

Willy is a bit like the Wizard, hidden from sight in his fortress-like factory at one end of town, while the young hero, Charlie Bucket (Freddie Highmore), starves with his family in a shack at the other. The inside of Willy's factory is a richly imagined version of the Land of Cockaygne, where unpredictable perils lurk behind every hyperbolical sweet.

We accordingly fear the worst when Charlie and four undeserving rich kids win a tour of Willy's kingdom. Re-tooled to represent gluttony, spoiled rottenness, hyper-competitiveness and addiction to videogame violence, Charlie's companions are clearly candidates for the medieval-style retribution that Mr Burton gleefully dishes out. Their fates are celebrated in four satirical songs written by the late Mr Dahl, set to music by Danny Elfman and performed by a chorus of Oompa-Loompas, Willy's pint-sized employees, all of whom are played by one diminutive Indian actor, Deep Roy.

Mr Burton's great star Johnny Depp plays Willy Wonka to rhyme with "bonkers", complete with a backstory about a dentist father (Christopher Lee) whose orthodontic torture devices have left him a child-man, prone to take his traumas out on his little guests. Critics have compared this Willy to everyone from Michael Jackson to Carol Channing, but he is basically a somewhat sinister version of the self-portraits of the artist as a young basket-case which Mr Depp has previously played for Mr Burton.

The father-son story plays out successfully, as it did in "Big Fish", another Burton movie also scripted by John August. The film is full of references to the director's other work. This time, he gives his rather cruel cautionary tale a happy ending. But shedding tragedy has impaired neither wit nor vision.

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The violins of Cremona

Lords of the strings

Jul 28th 2005 | VERMILLION, SOUTH DAKOTA
From The Economist print edition

Celebrating a mighty era of violin-making

FIVE HUNDRED years ago, give or take a year or two (nobody knows the exact date), Andrea Amati, the founding father of what would become the world's greatest school of violin-makers, was born in Cremona, a town in northern Italy. Violins had been built before Amati pioneered his instrument, but none had been built like his. Virtually unchanged since his death in 1577, the instrument he developed led composers and players to reroute the course of western music around violin-based ensembles.

Over the next 200 years or so, the torch passed to Amati's sons, grandson and great-grandson as well as to his even more illustrious successors, Antonio Stradivari and Giuseppe Guarneri. But by the mid-18th century, Cremona's fortunes were fading fast, and the violin trade with them. Yet the product that had made the town famous has remained as fresh, gorgeous and desirable as ever.

Always a collectable, it became a cultural icon. Now, with western prosperity and the ascent of the Asian rim, a Cremona violin has become a movable asset with a huge inflation rate. As late as the 1960s, a Stradivari violin could be had for under $100,000. In 1971, Sotheby's in London sold the “Lady Blunt” Strad for about $200,000. In April 2005, Christie's in New York sold the “Lady Tennant” Strad for more than $2m.

Museums, copyists, restorers and dealers watched with interest as the price of Stradivari violins soared, pulling along behind them the violins made by several dozen other Italian craftsmen working between the 16th and 18th centuries. Since credible authentication is crucial in the tiny but fiercely competitive oligopoly of high-stakes dealers, historical research has also prospered.

Since the 1970s, platoons of researchers, most hired by dealers, have combed the Cremona archives with a dedication and ingenuity that any graduate history department would be proud of. In fact, academia has never acknowledged the violin's rich history; virtually none of the researchers is a professional historian.

In 1995, their efforts paid off. Searching for traces of Guarneri, Carlo Chiesa and Duane Rosengard discovered Stradivari's will, dated 1729. Mr Chiesa is a Milanese violin-maker with an interest in historical reconstruction. Mr Rosengard is a bass player in the Philadelphia Orchestra, whose curiosity began with his own instrument. Their monograph, privately published by a London dealer, Peter Biddulph, in 1998, illuminates the master's investments, business associations and intra-family relationships better than anything written since 1902, when the Hill Brothers, a legendary family of dealers, published the standard biography.

For years, Claire Givens, a Minneapolis dealer, had dreamed of finding a place and an occasion to connect scholars and instruments with an audience that would appreciate them. Her hopes recently came to pass. The question of place was solved when she was appointed to the board of the National Music Museum in Vermillion, South Dakota. The occasion was seized with this year's anniversary, more or less, of Amati's birth. The consequence was that Independence Day this July was celebrated in a rather different way at the University of South Dakota.

Friends of the instrument gathered from near and far to take part in a four-day conference entitled “The Secrets, Lives and Violins of the Great Cremona Makers, 1505-1744”. Even Luigi Turletti, the immigrant Italian caterer, found it a bit odd to be honouring a Cremona native in South Dakota. But the exemplary collection of Amatis, Stradivaris and Guarneris that Vermillion acquired in the 1980s made the museum a natural for a Cremona show-and-tell.

The programme drew a capacity crowd of dealers, players, makers, musicologists and just plain violin geeks such as Lonnie Collins, a biker from Arkansas, with the 1737 “King Joseph” Guarneri tattooed on

his arm. The instruments were on view in a gallery across the hall. Joshua Koestenbaum, associate principal cellist of the Saint Paul Chamber Orchestra, and Sergiu Luca, an acclaimed early-music specialist, were invited to show them off.

The panelists, a top team of international researchers, addressed basic questions. What was it that made Cremona Cremona, and Amatis Amatis? Why did a phenomenon that began with a bang end with a whimper 300 years later?

There was general consensus that Amati's Cremona was a wealthy town in a wealthy country. Strategically located on major trade routes, it was easy to reach by land and water, and endowed with high quality wood, steel tools and a variety of skilled labour. Church, municipality and the private sector kept musicians busy. Changing taste favoured instruments that could be played louder and faster.

It was agreed that Amati's workmanship, materials and attention to geometry exceeded anything to date. According to John Dilworth, a London-based maker and historian, his use of reusable templates alone distinguished him from all his contemporaries.

The experts noted that Cremonese violin-making survived Stradivari and Carlo Bergonzi, the last of the great Cremonese masters who died in 1747. But the next lot of makers were only good, not great.

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Economist.com PRINT EDITION OBITUARY
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Obituary

General William Westmoreland

Jul 28th 2005
From The Economist print edition

AP

William Childs Westmoreland, soldier, died on July 18th, aged 91

THOUGH many tried to dissuade him, in 1974 William Westmoreland (General, US army, retired) ran for the governorship of South Carolina. He lost, and was not surprised. “I'm used to a structured organisation”, he confessed afterwards, “and this civilian process is so doggone nebulous.”

That word, for him, summed up the frustrations of a general's life in a democracy. During his years in Vietnam, as commander of American forces from 1964 to 1968, he had been fighting not only a subtle, nimble enemy hidden in villages and jungle, but a miasma of criticism, hatred and political timidity at home. He was never his own master, but the servant of Lyndon Johnson and his civilian advisers. He could not even choose where to direct the bombing of North Vietnam, since, as he growled in his memoirs, “this or that target was not to be hit for this or that nebulous non-military reason.”

General Westmoreland himself was the reverse of nebulous: tall, well-eyebrowed, jut-chinned, and with an impressive scar on his left cheek from hurtling through a windscreen as a child. His creed was “Duty, Honour, Country”, as drilled into every cadet at West Point. His approach to strategy was bluntly old-fashioned, not to say heavy-handed. The South Vietnamese army had to be structured as a conventional force, ready for large-scale military operations, even though it was fighting guerrillas. America needed to hit North Vietnam “surely, swiftly, and powerfully...with sufficient force to hurt”, as at Khe Sanh, where B-52s dropped more than 100,000 tonnes of bombs over two months. And troops needed to be poured in. General Westmoreland's tactics were simple: take the war to the enemy, and kill him faster than he could be replaced. Where possible, apply overwhelming, stunning force. “A great country”, he liked to say, quoting the Duke of Wellington, “cannot wage a little war.”

On General Westmoreland's watch, the numbers of Americans in South Vietnam rose from 15,000 military “advisers” in 1964 to 500,000 troops by 1968, and he wanted more. The conflict, he believed, was winnable. A combination of flawed intelligence, book-cooking, random “body-counts” and wishful thinking led to chronic underestimates of the strength of the enemy. He could win the war, he told Johnson early in 1968, if he had 206,000 extra men and if the reserves were mobilised. At this suggestion, Johnson's advisers sharply drew in breath. If this was what was needed to reach “the light at the end of the tunnel”, America could not do it. Within the year, General Westmoreland had been replaced, the bombing of the North moderated, and the scene set for talks.

He was blamed for losing the war, America's only defeat in its history. In his view, however, this “noble”

conflict was lost only in the public mind and in the pages of the *New York Times*. True, in April 1975 helicopters had winched the last Americans from the rooftops of Saigon as the city fell to the Vietcong; but this, in General Westmoreland's view, was a defeat for the South Vietnamese. American troops had not been bested in any engagement of significance. Instead, in 1973 the politicians had made them stop fighting, like a boxer who, with his opponent on the ropes, suddenly and inexplicably throws in the towel. They would certainly have won, the general insisted, if they had been allowed to expand operations into Laos, Cambodia and the North, disrupting chains of supply and recruitment to the Vietcong. But Johnson, fearing to stir up Russia or China, had never allowed it.

From horses to helicopters

The chaos and complexities of Vietnam were not what General Westmoreland had been trained for. On his graduation in 1936, as an artillery officer, the big guns he encountered were Model 1897 French 75s with steel-rimmed wooden wheels, drawn by horses. His great-uncle, who had fought for the Confederacy with many other ardent South Carolinians, would have recognised this style of warfare. General Westmoreland, however, came to shape modern ways of fighting, especially with his massive use of helicopter gunships to gain mobility in battle. These, flying in assault formation, became the motif of the Vietnam war.

In a less controversial conflict, General Westmoreland might have been given more credit. He took care of his men, to the point of parachuting first from aircraft in case the wind was dangerous. He believed in keeping up morale with copious medals and commendations (his commendation of Charlie Company, after its infamous torching and massacre of the village of My Lai, being an unfortunate mistake). But he was not forgiven for his rosy forecasts of how the war would go. He became army chief of staff, but was never promoted to the joint chiefs. As the war dragged on into the Nixon years, he was rarely sought for his advice.

Reporters sometimes asked what he thought of his “counterpart” on the North Vietnamese side, Vo Nguyen Giap. He bristled at that: not because he thought him a bad soldier or a bad man, but because Giap had been a powerful member of his government, and had been able to impose his wishes on the rest. Not so General Westmoreland, defeated by a cloud.

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Overview

Jul 28th 2005
From The Economist print edition

In **America** sales of existing homes surged to a record annual rate of 7.33m in June. Sales of apartments were particularly strong, up by nearly 40% at an annual rate in the second quarter. The median price of homes rose by 14.7% in the year to June, the biggest increase since November 1980.

Britain's GDP grew by only 0.4% in the second quarter, reducing its year-on-year growth rate to 1.7%, its weakest pace since 1993, when the economy was just emerging from recession.

Things are looking rosier for companies in **continental Europe**. In July, surveys of business confidence rose by more than expected in Germany, France and Italy. However, Belgium's GDP rose by only 1.4% in the year to the second quarter.

Germany's 12-month consumer-price inflation rate rose to 1.9% in July, up from 1.6% in June, largely due to a jump in oil prices. **Canada's** 12-month inflation rate edged up to 1.7% in June; **Australia's** rose to 2.5% over the same period.

Japanese consumers have started to open their wallets again. Retail sales rose by 2.8% in the 12 months to May.

Wages in **Italy** rose by 3.0% in the year to June, well ahead of inflation. In contrast, German wages rose by only 0.6% in the year to May, implying a pay cut in real terms.

Revised figures for *The Economist*'s world GDP indicator show that **global GDP** growth slowed to 4.1% in the first quarter of 2005, down from 5.3% a year earlier, but still above its long-term average growth rate.

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Output, demand and jobs

Jul 28th 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 1.9	Q1	+ 2.8	+ 2.4	+ 3.1	+ 1.2	Q1	+ 1.8	Q1	5.0	Jun	5.6
Austria	+ 2.0	Q1	+ 0.8	+ 1.9	+ 2.0	+ 3.2	Apr	– 2.4	Apr	4.6	Jun	4.2
Belgium	+ 1.4	Q2	+ 1.2	+ 1.2	+ 1.9	+ 1.1	May	+ 3.4	Apr	12.2	May†	12.3
Britain	+ 1.7	Q2	+ 1.5	+ 2.2	+ 2.2	– 1.9	May	+ 1.7	Jun	4.8	May††	4.8
Canada	+ 3.3	Q1	+ 2.3	+ 2.8	+ 3.0	+ 1.7	Apr	+ 6.4	Apr	6.7	Jun	7.2
Denmark	+ 0.8	Q1	+ 0.6	+ 2.1	+ 2.2	+ 2.0	May	+ 8.7	May	5.8	Jun	6.5
France	+ 1.8	Q1	+ 1.4	+ 1.5	+ 1.9	– 0.2	May	+ 1.5	May	10.2	May	10.0
Germany	+ 1.1	Q1	+ 4.2	+ 1.1	+ 1.3	+ 0.8	May	+ 2.7	May	11.6	Jul§	10.6
Italy	– 0.2	Q1	– 1.8	– 0.2	+ 1.1	– 2.1	May	– 4.6	Apr	7.8	Mar	8.2
Japan	+ 1.3	Q1	+ 4.9	+ 1.6	+ 1.8	+ 0.3	May	+ 3.1	Jun	4.4	May	4.6
Netherlands	– 0.5	Q1	– 3.2	+ 0.5	+ 1.5	– 1.0	May	– 2.8	Apr	6.7	Jun**	6.4
Spain	+ 3.3	Q1	+ 3.5	+ 3.1	+ 2.8	+ 0.5	May	+ 1.4	Jun	9.9	May	11.1
Sweden	+ 1.4	Q1	+ 1.1	+ 1.9	+ 2.6	– 0.9	May	+ 9.6	Jun	5.2	May†	5.7
Switzerland	+ 0.8	Q1	+ 0.2	+ 0.9	+ 1.5	– 0.3	Q1	– 0.4	May	3.6	Jun†	3.7
United States	+ 3.7	Q1	+ 3.8	+ 3.5	+ 3.2	+ 3.9	Jun	+ 4.3	May	5.0	Jun	5.6
Euro area	+ 1.4	Q1	+ 1.9	+ 1.3	+ 1.7	+ 0.1	May	+ 2.0	May	8.8	May	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.0	Q1	+ 0.5	na	na	– 7.5	May	+ 6.3	May	8.7	Jun†	8.9
Greece	+ 3.5	Q1	na	na	na	– 2.3	May	+ 3.5	Apr	10.2	Dec	9.8
Iceland	+ 2.9	Q1	na	na	na	na		na		2.2	May†	3.3
Ireland	+ 2.8	Q4	na	na	na	– 3.4	May	+ 4.6	May	4.2	Jun	4.4
Luxembourg	+ 3.1	Q1	na	na	na	+ 4.6	Apr	– 3.5	May	4.5	May	3.9
New Zealand	+ 1.9	Q1	+ 1.5	na	na	+ 3.5	Q4	+ 5.8	Q1	3.9	Q1	4.2
Norway	– 0.8	Q1	+ 2.2	na	na	+ 0.1	May	+ 7.2	May	4.6	May**	4.3
Portugal	+ 0.1	Q1	+ 0.8	na	na	– 4.7	May	+ 2.5	May	7.5	Q1†	6.4

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Mar-May; claimant count rate 2.8% in Jun.
§EU harmonised rate 9.3% in May. **Apr-Jun.

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Prices and wages

Jul 28th 2005
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2005	2006	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 2.5	Q2	+ 2.5	+ 2.7	+ 2.6	+ 6.9	Q2	+ 2.8	+ 4.5	Q1	+ 5.0
Austria	+ 2.3	Jun	+ 2.3	+ 2.1	+ 1.7	+ 0.7	Jun	+ 5.9	+ 2.2	Jun	+ 2.2
Belgium	+ 2.9	Jun	+ 2.3	+ 2.1	+ 1.7	+ 2.4	May	+ 3.9	+ 2.6	Apr	+ 2.3
Britain	+ 2.0	Jun*	+ 1.6	+ 1.9	+ 1.9	+ 2.4	Jun	+ 2.6	+ 4.1	May†	+ 4.6
Canada	+ 1.7	Jun	+ 2.5	+ 2.1	+ 2.2	– 0.3	May	+ 6.4	+ 3.1	Apr	+ 3.3
Denmark	+ 1.8	Jun	+ 1.1	+ 1.4	+ 1.7	+ 3.9	Jun	+ 2.4	+ 3.1	Q1	+ 3.3
France	+ 1.7	Jun	+ 2.4	+ 1.7	+ 1.6	+ 2.9	Jun	+ 2.2	+ 2.9	Q1	+ 2.8
Germany	+ 1.9	Jul	+ 1.8	+ 1.4	+ 1.1	+ 2.2	Jun	+ 3.5	+ 0.6	May	+ 1.9
Italy	+ 1.8	Jun	+ 2.4	+ 2.0	+ 1.9	+ 3.7	Jun	+ 3.2	+ 3.0	Jun	+ 3.3
Japan	+ 0.2	May	– 0.5	– 0.1	+ 0.2	+ 1.4	Jun	+ 1.5	– 0.2	May	+ 2.2
Netherlands	+ 1.6	Jun	+ 1.4	+ 1.4	na	+ 3.3	May	+ 4.2	+ 0.6	Jun	+ 1.4
Spain	+ 3.3	Jul	+ 3.4	+ 3.0	+ 2.7	+ 4.4	Jun	+ 4.0	+ 3.0	Q1	+ 3.2
Sweden	+ 0.6	Jun	+ 0.5	+ 0.5	+ 1.4	+ 3.2	Jun	+ 1.5	+ 1.3	Apr	+ 2.9
Switzerland	+ 0.7	Jun	+ 1.1	+ 1.1	+ 1.1	+ 0.5	Jun	+ 1.5	+ 0.9	2004	+ 1.4
United States	+ 2.5	Jun	+ 3.3	+ 2.9	+ 2.5	+ 3.6	Jun	+ 4.3	+ 2.7	Jun	+ 2.0
Euro area	+ 2.1	Jun	+ 2.4	+ 1.9	+ 1.5	+ 3.5	May	+ 2.4	+ 3.1	Q1	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.1	Jun	– 0.1	na	na	+ 4.0	Jun	+ 1.0	+ 4.1	Q1	+ 4.2
Greece	+ 3.3	Jun	+ 2.8	na	na	+ 3.0	May	+ 6.0	na		na
Iceland	+ 3.5	Jul	+ 3.6	na	na	+ 3.7	Jul	+ 5.3	+ 6.3	Jun	+ 5.1
Ireland	+ 2.1	Jun	+ 2.3	na	na	– 0.3	Jun	+ 1.3	+ 6.4	Q1	+ 3.9
Luxembourg	+ 2.2	Jun	+ 2.6	na	na	+ 6.7	May	+ 7.7	+ 0.4	Apr	+ 4.7
New Zealand	+ 2.8	Q2	+ 2.4	na	na	+ 4.2	Q1	– 0.6	+ 2.5	Q1	+ 2.2
Norway	+ 1.7	Jun	+ 1.3	na	na	+19.3	Jun	+12.0	+ 3.7	Q1	+ 3.5
Portugal	+ 1.6	Jun	+ 2.7	na	na	+ 3.7	Jun	+ 2.3	– 3.0	May	+ 0.8

*RPI inflation rate 2.9% in Jun. †Mar-May.

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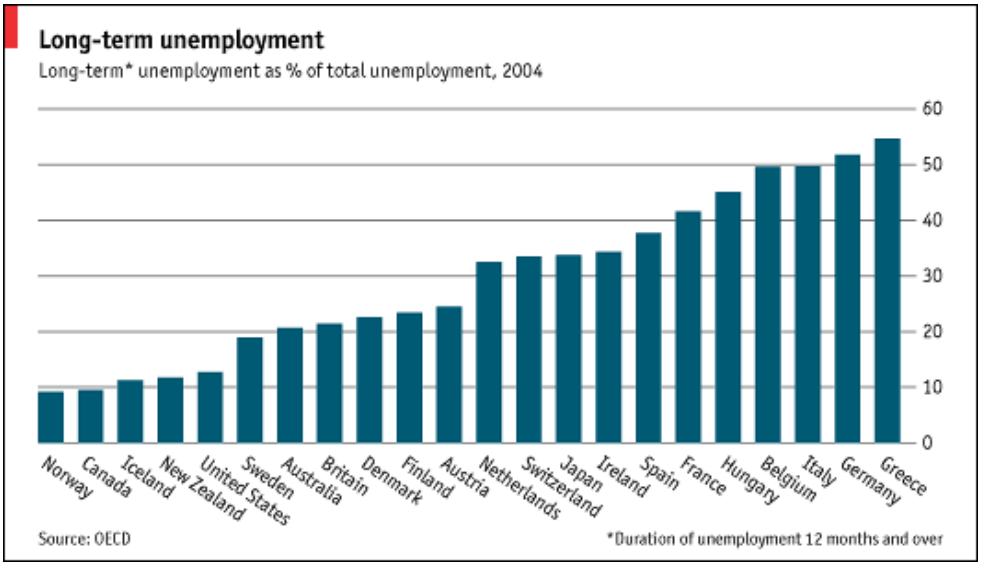
Long-term unemployment

Jul 28th 2005
From The Economist print edition



Unemployment can be lengthy, even in countries where it is low. Japan, for example, has a lower unemployment rate than America and Britain. But over a third of Japan's jobless have been out of work for a year or more, compared with 21.4% in Britain and just 12.7% in America. The skills of the long-term unemployed may atrophy over time, leaving them less able to compete in the labour market.

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Money and interest rates

Jul 28th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Jul 27th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 5.4	+ 9.2	May	5.65	5.47	5.17	5.17	5.89	6.18
Britain	+ 3.7	+11.0	Jun	4.56	4.88	4.11	4.29	5.17	5.19
Canada	+ 8.4	+10.4	Jun	2.57	2.09	2.99	3.97	4.89	5.26
Denmark	+21.3	+16.8	Jun	2.20	2.25	2.14	3.17	4.39	4.92
Japan	+ 4.4	+ 1.7	Jun	0.02	0.03	0.08	1.29	1.84	1.35
Sweden	+ 1.8	+ 9.4	Jun	1.45	1.99	1.88	2.99	4.56	2.66
Switzerland	– 2.5	+ 4.7	Jun	0.75	0.53	0.91	1.93	2.88	1.88
United States	+ 2.1	+ 4.8	Jun	3.49	1.53	3.94	4.26	4.58	5.16
Euro area†	+10.5	+ 7.5	Jun	2.13	2.12	2.19	3.19	4.25	3.42

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.47%, Japan No. 271 1.30%. Central bank rates: US fed funds 3.25%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.75%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jul 28th 2005
From The Economist print edition

2000=100

	Jul 19th	Jul 26th*	% change on one month	% change on one year
Dollar index				
All items	134.3	134.8	+ 1.0	+ 8.0
Food	128.9	128.7	– 0.1	+ 6.1
Industrials				
All	141.3	142.6	+ 2.3	+10.3
Nfa†	135.4	135.2	+ 2.5	+ 2.4
Metals	144.5	146.6	+ 2.2	+14.6
Sterling index				
All items	117.2	117.3	+ 5.4	+13.1
Euro index				
All items	103.6	103.7	+ 1.5	+ 8.3
Yen index				
All items	140.8	140.4	+ 3.3	+ 9.2
Gold				
$ per oz	426.65	424.30	– 2.8	+ 9.3
West Texas Intermediate				
$ per barrel	57.45	59.10	+ 1.5	+41.3

* Provisional. † Non-food agriculturals.

Our commodity-price index was rebased in February 2005.

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Stockmarkets

Jul 28th 2005
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Market indices

	Jul 27th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,347.6	4,347.6	3,905.5	+ 2.0	nil	+ 7.3	+ 3.3
Austria (ATX)	3,080.4	3,099.5	2,415.0	+ 0.3	- 0.6	+26.7	+12.2
Belgium (Bel 20)	3,217.8	3,217.8	2,958.8	+ 1.0	-12.6	+ 9.7	- 2.8
Britain (FTSE 100)	5,263.6	5,270.7	4,783.6	+ 0.9	-24.0	+ 9.3	- 0.8
Canada (Toronto Composite)	10,500.7	10,500.7	9,006.2	+ 1.7	- 7.8	+13.6	+10.0
Denmark (KBX)	318.7	318.7	257.8	+ 1.6	nil	+23.6	+ 9.1
France (SBF 250)	3,079.5	3,079.5	2,633.6	+ 0.5	-29.9	+16.9	+ 3.5
(CAC 40)	4,433.1	4,433.1	3,816.1	+ 0.3	-36.0	+16.0	+ 2.8
Germany (DAX)*	4,855.4	4,855.4	4,178.1	+ 1.5	-39.8	+14.1	+ 1.0
Italy (S&P/MIB)	33,658.0	33,658.0	30,645.0	+ 0.6	-32.8	+ 8.9	- 3.5
Japan (Nikkei 225)	11,835.1	11,966.7	10,825.4	+ 0.4	-69.6	+ 3.0	- 6.0
(Topix)	1,199.0	1,203.3	1,109.2	+ 0.2	-58.4	+ 4.3	- 4.8
Netherlands (AEX)	395.1	397.0	347.0	- 0.1	-43.7	+13.5	+ 0.5
Spain (Madrid SE)	1,089.9	1,089.9	950.9	+ 0.7	- 4.9	+13.6	+ 0.6
Sweden (Affarsvarlden Gen)	259.1	259.1	218.9	+ 1.3	-35.3	+17.1	- 0.8
Switzerland (Swiss Market)	6,560.1	6,560.1	5,669.6	+ 0.8	-22.0	+15.2	+ 0.9
United States (DJIA)	10,637.1	10,940.6	10,012.4	- 0.5	- 9.3	- 1.4	- 1.4
(S&P 500)	1,236.8	1,236.8	1,137.5	+ 0.1	-19.0	+ 2.1	+ 2.1
(NASDAQ Comp)	2,186.2	2,188.6	1,904.2	- 0.1	-56.7	+ 0.5	+ 0.5
Europe (FTSEurofirst 300)†	1,173.8	1,173.8	1,038.6	+ 0.9	-31.2	+12.7	- 0.2
Euro area (FTSE Euro 100)†	1,007.7	1,007.7	894.4	+ 0.4	-35.0	+11.9	- 0.9
World (MSCI)‡	1,183.3	1,193.0	1,115.0	+ 0.6	-18.3	+ 1.2	+ 1.2
World bond market (Citigroup)††	630.3	662.3	626.9	+ 0.6	- 4.8	- 5.4	- 5.4

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jul 28th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Jul 27th	year ago	Currency units per $ Jul 27th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 18.1	May	− 42.4	Q1	− 5.8	− 5.5	118.1	109.4	1.32	1.43	2.31	1.59	1.18	+ 0.9
Austria	− 1.6	May	+ 0.5	May	− 0.4	− 0.4	104.5§	103.9	0.83	0.83	1.45	–	0.74	− 2.0
Belgium	+ 16.5	May	+ 12.2	Mar	+ 3.0	+ 3.0	105.2§	104.3	0.83	0.83	1.45	–	0.74	− 0.5
Britain	−111.9	May	− 44.0	Q1	− 2.4	− 2.5	97.6	102.6	0.57	0.55	–	0.69	0.51	− 2.9
Canada	+ 47.5	May	+ 20.2	Q1	+ 1.3	+ 1.1	117.1	108.7	1.24	1.33	2.16	1.49	1.10	+ 1.2
Denmark	+ 9.2	May	+ 11.0	May	+ 2.0	+ 1.9	106.0	105.9	6.20	6.18	10.8	7.46	5.52	+ 1.8
France	− 26.0	May	− 24.6	May	− 0.6	− 0.3	107.8§	106.8	0.83	0.83	1.45	–	0.74	− 3.0
Germany	+195.8	May	+105.7	May	+ 3.5	+ 3.3	105.7§	104.5	0.83	0.83	1.45	–	0.74	− 3.5
Italy	− 6.8	May	− 21.5	May	− 1.2	− 1.3	77.2§	76.5	0.83	0.83	1.45	–	0.74	− 4.4
Japan	+115.9	May	+167.8	May	+ 3.6	+ 3.5	85.7	86.2	112	112	196	135	–	− 6.1
Netherlands	+ 40.7	May	+ 33.9	Q1	+ 3.7	+ 3.6	104.6§	103.7	0.83	0.83	1.45	–	0.74	− 2.2
Spain	− 88.1	May	− 69.9	Apr	− 5.2	− 5.3	77.6§	77.2	0.83	0.83	1.45	–	0.74	+ 0.5
Sweden	+ 22.5	Jun	+ 29.7	Q1	+ 7.0	+ 6.4	95.1	97.0	7.84	7.67	13.7	9.44	6.98	+ 0.8
Switzerland	+ 7.3	Jun	+ 40.2	Q1	+11.4	+10.8	105.7	107.1	1.30	1.28	2.26	1.56	1.16	− 1.0
United States	−717.9	May	−717.0	Q1	− 6.3	− 6.2	87.0	88.2	–	–	1.74	1.20	0.89	− 4.1
Euro area	+ 63.5	May	+ 27.9	Apr	+ 0.5	+ 0.4	116.1	114.4	0.83	0.83	1.45	–	0.74	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 12.8	May	+ 6.5	May	na	na	82.1§	81.4	0.83	0.83	1.45	–	0.74	+ 1.3
Greece	− 33.5	Apr	− 15.7	May	na	na	60.2§	59.8	0.83	0.83	1.45	–	0.74	− 3.8
Iceland	− 0.8	May	− 1.4	Q1	na	na	109.0**	96.5	64.8	71.7	113	78.0	57.7	+ 1.1
Ireland	+ 40.9	May	− 3.1	Q1	na	na	95.3§	93.8	0.83	0.83	1.45	–	0.74	− 0.7
Luxembourg	− 4.3	Apr	+ 3.0	Q1	na	na	105.2§	104.3	0.83	0.83	1.45	–	0.74	− 0.8
New Zealand	− 3.4	May	− 7.0	Q1	na	na	134.5	125.3	1.47	1.59	2.56	1.77	1.31	+ 3.2
Norway	+ 40.4	Jun	+ 37.9	Q1	na	na	110.6	102.8	6.58	7.01	11.5	7.92	5.86	+ 14.4
Portugal	− 20.1	Apr	− 15.3	May	na	na	94.5**	93.6	0.83	0.83	1.45	–	0.74	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, May average. ‡OECD forecast. **IMF, March average.

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The world's biggest companies

Jul 28th 2005
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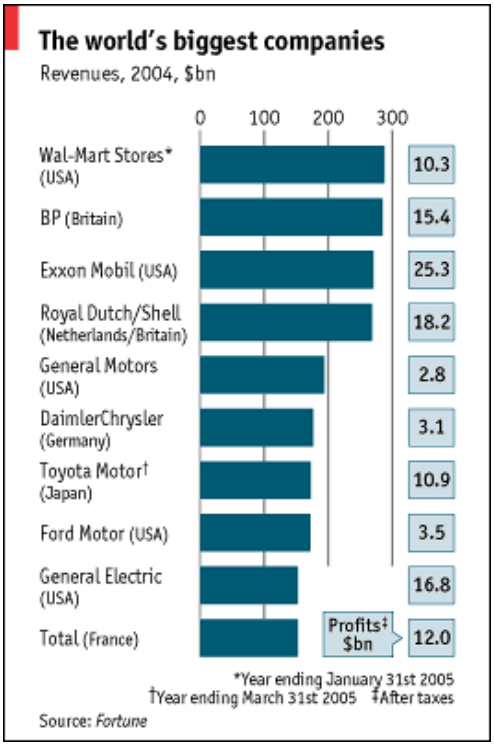

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Overview

Jul 28th 2005
From The Economist print edition

South Korea's GDP grew by 1.2% in the second quarter of this year, its biggest increase since 2003, thanks to a revival of consumer spending and investment. The year-on-year growth rate rose to 3.3%.

Brazil had a current-account surplus of $12.6 billion in the 12 months to June. This was smaller than in May, but still almost twice as large as a year ago.

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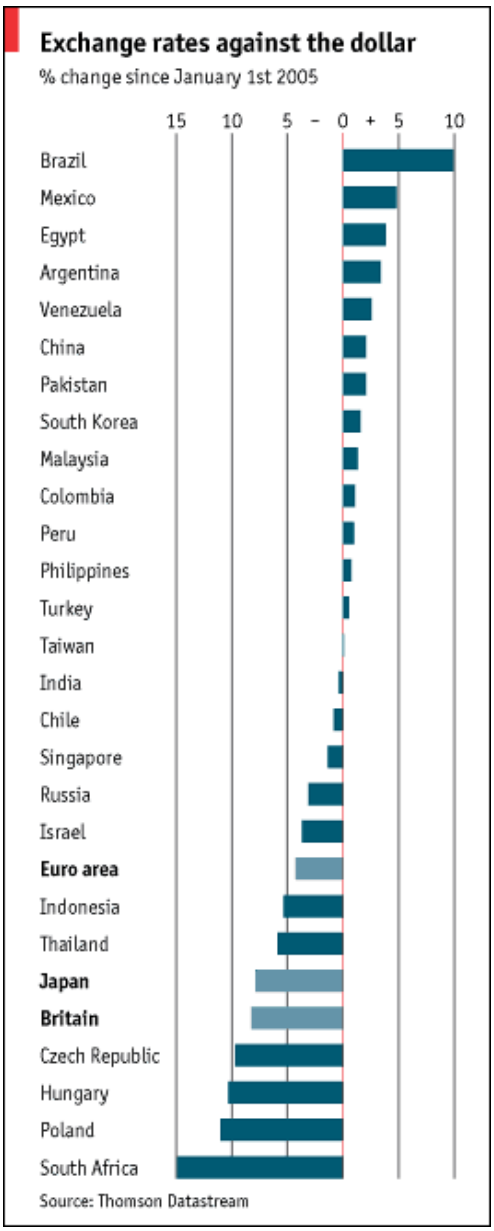
Exchange rates against the dollar

Jul 28th 2005
From The Economist print edition

On July 21st, China abandoned its long-standing currency peg of 8.28 to the dollar, revaluing the yuan by 2.1%. Malaysia followed suit, dropping its seven-year-old dollar peg and letting the ringgit appreciate by more than 1%. Since the beginning of the year, about half of the emerging-market currencies in our chart have risen against the dollar. Brazil's *real* posted the biggest gains, climbing by almost 10%. The South African rand, by contrast, lost 15% of its value against the dollar.



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Economy

Jul 28th 2005
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.5	Q2	+16.8	Jun	+ 1.6	Jun	+79.2	Jun	+68.7	2004	711.0	Jun
Hong Kong	+ 6.0	Q1	– 0.6	Q1	+ 1.2	Jun	– 9.7	Jun	+18.5	Q1	122.0	Jun
India	+ 7.0	Q1	+10.8	May	+ 3.7	May	–32.4	Jun	– 6.4	Q1	127.0	Jun
Indonesia	+ 6.4	Q1	+10.1	Mar	+ 7.4	Jun	+27.6	May	+ 7.8	Q1	33.3	May
Malaysia	+ 5.7	Q1	– 0.4	May	+ 3.2	Jun	+23.2	May	+16.7	Q1	74.1	May
Philippines	+ 4.6	Q1	+ 2.5	Apr	+ 7.6	Jun	– 0.1	May	+ 2.9	Mar	15.1	Jun
Singapore	+ 3.9	Q2	+11.1	Jun	– 0.2	Jun	+16.3	Jun	+29.2	Q1	115.2	Jun
South Korea	+ 3.3	Q2	+ 4.1	Jun	+ 2.7	Jun	+27.0	Jun	+23.0	May	204.1	Jun
Taiwan	+ 2.5	Q1	+ 1.3	Jun	+ 2.4	Jun	+ 2.7	Jun	+16.9	Q1	253.6	Jun
Thailand	+ 3.3	Q1	+ 8.0	May	+ 3.8	Jun	– 4.4	May	+ 0.1	May	47.1	May
Argentina	+ 8.0	Q1	+ 2.0	Jun	+ 9.0	Jun	+11.2	May	+ 2.8	Q1	21.4	May
Brazil	+ 2.9	Q1	+ 5.5	May	+ 7.3	Jun	+38.3	Jun	+12.6	Jun	60.7	May
Chile	+ 5.7	Q1	+ 6.8	May	+ 2.7	Jun	+ 9.0	Jun	+ 1.1	Q1	16.6	Jun
Colombia	+ 3.6	Q1	+ 2.1	May	+ 4.8	Jun	+ 1.5	Apr	– 0.8	Q1	12.5	Jun
Mexico	+ 2.4	Q1	+ 3.0	May	+ 4.3	Jun	– 9.8	Jun	– 8.7	Q1	61.9	May
Peru	+ 7.1	May	+ 9.1	May	+ 1.5	Jun	+ 3.5	May	+ 0.4	Q1	13.0	Jun
Venezuela	+ 7.9	Q1	+28.2	Apr	+15.9	Jun	+22.6	Q1	+14.9	Q1	22.3	May
Egypt	+ 4.7	Q4	+ 3.3	2004†	+ 5.0	May	– 9.5	Q1	+ 4.4	Q1	17.6	Jun
Israel	+ 4.1	Q1	+ 5.2	May	+ 0.3	Jun	– 7.6	Jun	+ 1.9	Q1	26.5	Jun
South Africa	+ 4.2	Q1	+ 1.2	May	+ 2.8	Jun	– 2.7	May	– 8.5	Q1	16.9	Jun
Czech Republic	+ 4.4	Q1	+ 4.0	May	+ 1.8	Jun	+ 0.7	May	– 4.4	Q1	30.1	Jun
Hungary	+ 2.9	Q1	+10.1	May	+ 3.8	Jun	– 2.7	Q1	– 9.2	Q1	17.1	Jun
Poland	+ 2.1	Q1	+ 0.9	May	+ 1.4	Jun	– 3.6	May	– 1.0	May	39.3	May
Russia	+ 5.2	Q1	+ 6.9	Jun	+13.3	Jun	+105.5	May	+69.2	Q1	147.8	Jun
Turkey	+ 4.8	Q1	+ 2.1	May	+ 9.0	Jun	–37.4	May	–18.2	May	35.8	May
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 7.2	Q1	+ 8.4	May	+ 3.1	Jun	– 2.4	May	– 1.3	May	1.7	May
Latvia	+ 7.4	Q1	+ 9.9	May	+ 6.3	Jun	– 2.7	May	– 1.6	May	2.0	May
Lithuania	+ 8.2	Q2	na		+ 2.0	Jun	– 3.1	May	– 1.5	Q1	3.5	May
Slovakia	+ 5.1	Q1	+ 1.5	May	+ 2.5	Jun	– 2.1	May	– 1.9	Mar	15.7	May
Slovenia	+ 2.6	Q1	+ 1.3	May	+ 1.9	Jun	– 1.3	May	nil	May	8.4	Apr
Pakistan	+ 6.4	2004†	+ 9.6	Jan	+ 8.7	Jun	– 6.2	Jun	– 1.5	Q1	10.4	May
Saudi Arabia	+ 5.2	2004	na		+ 0.6	Mar	+84.9	2004	+51.5	2004	26.7	May

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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Financial markets

Jul 28th 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jul 27th		Dec 31st 2004	
	Jul 27th	year ago	Jul 27th	% a year		one week	in local currency	in $ terms
China	8.11	8.28	14.1	2.00	1,145.8	+6.7	– 13.9	– 12.1
Hong Kong	7.78	7.80	13.6	3.54	14,801.9	+1.4	+ 4.0	+ 3.9
India	43.5	46.3	75.7	5.47	7,605.0	+3.6	+ 15.2	+ 15.2
Indonesia	9,840	9,120	17,146	8.85	1,178.1	+3.3	+ 17.8	+ 11.1
Malaysia	3.75	3.80	6.54	2.88	932.0	+0.9	+ 2.7	+ 4.0
Philippines	56.1	56.0	97.8	6.75	1,974.5	+1.5	+ 8.3	+ 8.3
Singapore	1.67	1.73	2.90	2.00	2,333.6	+1.1	+ 12.9	+ 10.7
South Korea	1,031	1,168	1,797	3.49	1,093.0	+1.7	+ 22.0	+ 22.5
Taiwan	32.0	34.0	55.7	1.45	6,327.3	–1.5	+ 3.1	+ 2.2
Thailand	41.7	41.4	72.7	3.05	665.7	+2.4	– 0.4	– 7.2
Argentina	2.86	2.97	4.99	6.88	1,502.9	+1.0	+ 9.3	+ 13.5
Brazil	2.45	3.06	4.26	19.75	25,337.8	–1.4	– 3.3	+ 5.0
Chile	564	643	983	3.84	9,885.1	+1.7	+ 10.3	+ 8.7
Colombia	2,314	2,637	4,032	7.05	6,053.5	+2.3	+ 39.3	+ 41.6
Mexico	10.6	11.5	18.6	9.63	14,173.4	–0.9	+ 9.7	+ 14.9
Peru	3.25	3.42	5.67	3.02	4,210.8	+1.3	+ 13.5	+ 14.4
Venezuela	2,510§	2,656§	4,374	10.94	20,927.1	–1.8	– 30.1	– 28.2
Egypt	5.78	6.20	10.06	8.97	42,051.3	–3.4	+ 71.0	+ 79.8
Israel	4.55	4.53	7.93	3.59	700.0	+1.7	+ 8.7	+ 3.2
South Africa	6.65	6.29	11.6	7.10	15,120.5	+1.6	+ 19.5	+ 1.3
Czech Republic	25.1	26.3	43.8	1.80	1,258.2	+1.4	+ 21.9	+ 8.3
Hungary	204	206	355	6.59	20,523.3	+2.7	+ 39.2	+ 23.6
Poland	3.41	3.66	5.94	4.68	29,870.1	+1.2	+ 12.1	– 1.4
Russia	28.7	29.1	50.0	13.00	770.6‡	+1.7	+ 29.9	+ 25.5
Turkey	1.34	1.49	2.34	16.36	29,164.8	+1.6	+ 16.8	+ 17.4
EM (MSCI)*	1.00	1.00	1.74	na	594.1	+0.8	+ 9.6	+ 9.6
EMBI+†	1.00	1.00	1.74	na	345.6	–0.4	+ 4.9	+ 4.9

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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